PRE - BUDGET MEMORANDUM 2022-23

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PREAMBLE

The outbreak of second wave of COVID-19 witnessed during this year has had severe consequences on the economy in terms of the unprecedented health, social and economic impacts of the pandemic. Countries around the world are implementing economic and fiscal policy stimuli, including tax measures to support their economies under the COVID-19 pandemic. Considering the severity of adversity caused by the second wave and continuity of COVID-19 pandemic, the Government has from time to time provided various relaxations in terms of timelines for compliances specified under the tax laws, announced various relief measures pertaining to customs duty exemptions on COVID-19 related medical goods, rationalization of late fee for delay in filing GST returns etc. We commend the efforts made by the Government to announce these measures at an appropriate time.

Recently, the Government also took an appropriate move by ending the retrospective applicability of tax on indirect share transfers. This action will put the entire indirect transfer tax controversy to rest forever and will also play an important role in assuaging the concerns that investors have and will restore the credibility of the Indian tax and judicial system. However, the recent trend of having retrospective amendments in the tax laws viz. amendment pertaining to retrospective amendment to section 50B of the Act requiring fair market value of an undertaking to be considered as the full value of consideration for slump sale transactions, denying depreciation on goodwill from AY 2021-22, expanding the scope of equalization levy, that too, at the enactment stage of the Finance Bill, 2020. The retrospective nature of the amendment impacts the past business transactions and is contrary to the professed policy of current Government of not making retrospective amendments prejudicial to the taxpayers.

It is therefore important to have fair, stable, and predictable tax policies that can be effectively leveraged to spur consumption, growth, and investor sentiment.

The specific suggestions on the direct and indirect tax side for the consideration of the Government are set out in this Memorandum. We have however highlighted a few important issues for consideration of the Government: -

1. **Extend Cut Off Date for Commencing Manufacturing Operations under concessional tax regime of section 115BAB of the Act from March 31, 2023 to March 31, 2025**

As per Section 115BAB of the Income-tax Act, 1961 (‘the Act’), income-tax payable in respect of the total income of domestic company, for any previous year relevant to the assessment year beginning on or after the 1st day of April, 2020, shall be at the rate of 15%, if certain conditions specified thereunder are fulfilled. One of the conditions to avail the beneficial rate of 15% inter-alia is that the company should be incorporated on or after 1st October, 2019 and it should commence manufacturing or production of an article or thing on or before the 31st day of March, 2023.

Due to the outbreak of Covid-19 pandemic immediately after formation of these new companies, and considering the uncertainties involved around the same, the setting up of

manufacturing facilities/ production plans, regulatory approvals, resource planning are delayed until the situation is restored to normal.

New companies have been incorporated to undertake manufacturing and production facilities in order to avail the benefit of concessional tax rate and in line with governments thrust on setting up new domestic manufacturing facilities. As setting up the manufacturing /production facilities take considerable amount of time and capital investment and other works around the same, due to out-break of Covid 19 pandemic, it is likely that most of the projects may have an unexpected delay in the completion. Therefore, it is requested that suitable extension to commence the production / manufacturing facilities may be provided.

Considering the current scenario, that the economic activities are reverting to normalcy after almost 18 months, it is recommended that two-years extension to be granted to newly incorporated domestic companies to commence their manufacturing or production facilities till 31st Day of March, 2025 in order to avail the benefit of concessional tax rate.

2. Allow depreciation of goodwill in respect of for transactions completed prior to 1 April 2021 and for purchased goodwill in non-tax neutral transactions

The Finance Act 2021 made far reaching amendment of denying depreciation on goodwill, an issue which was in a way settled by the Supreme Court in the favour of the taxpayers. It is significant to note that while in legal form, the amendment was stated to be prospective i.e. it took effect from 1 April 2021 and applied from A.Y. 2021-22 onwards. However, in substance, the denial of depreciation has a retrospective impact on past business transactions and is contrary to the professed policy of current Government of not making retrospective amendments prejudicial to the taxpayers.

The amendment has far reaching adverse impact on industry and businesses which had so far arranged their affairs on the basis that goodwill will be allowed depreciation for tax purposes – at least for acquisition in non-tax neutral transaction. The pricing of the deals, fair exchange ratio between shares of amalgamating/demerged and amalgamated/resulting companies, indemnities provided by sellers, etc. were all based on admissibility of tax depreciation on goodwill in the hands of the buyer – at least on purchased goodwill. The Explanatory Memorandum to the Bill itself acknowledges that there is ‘valid claim’ of depreciation on purchased goodwill in view of Smifs ratio.

It is requested to at least make the amendment on prospective basis such that depreciation is denied only to goodwill acquired on or after 1 April 2021 and goodwill acquired in past (whether in tax neutral or taxable transaction) is ‘grandfathered’. Without prejudice, the denial of depreciation on goodwill acquired in taxable transaction needs reconsideration.

3. Incentivize generation of employment

Section 80JJAA of the Act allows deduction in respect of 30% of the salary of an additional employee hired during the year for a total period of three years. For this purpose, an additional employee is defined as one whose salary emoluments do not exceed Rs. 25,000 per month. Such threshold, even when introduced in 2016, was considered too low for granting any meaningful benefit. Subsequently, rising inflation and corresponding cost-of-

living, have rendered the deduction almost insignificant, thereby contradicting the policy intention of curtailing the unemployment rate in India by incentivizing hiring additional labour. The monetary limit of Rs. 25,000 per month does not provide incentive for hiring technically qualified skilled employees who provide more value addition to the business.

To keep pace with rising costs, as well as to incentivize hiring of employees in these uncertain times where the pandemic has led to severe downsizing, it is recommended to raise the threshold limit of monthly emoluments from Rs. 25,000 per month to Rs. 1 Lakh per month.

4. Provide clarifications with respect to Equalisation Levy

As per the Explanation to section 164(cb) of Finance Act, 2016, “e-commerce supply or service”, “online sale of goods” and “online provision of services” shall include one or more of the following online activities, namely: (a) Acceptance of offer for sale; or (b) Placing the purchase order; or (c) Acceptance of the purchase order; or (d) Payment of consideration; or (e) Supply of goods or provision of services, partly or wholly.

The expanded scope of the Explanation unduly covers other transactions which are traditionally not in the nature of e-commerce or digital transactions, such as intra-trading of goods where Indian entities purchase physical goods from their group entities outside India by placing a request on the ERP system of the group and goods are thereafter physically shipped into India, transactions where IT/ITES services, other support services, etc. are provided by overseas entities to their Indian group entities, where the actual services in many cases are predominantly rendered offline and transactions where the principal activity is carried out physically (i.e. offline) and merely placement/acceptance, or in some cases transmission of the final deliverable, is made online.

Considering that the objective of the EL provisions is to cover foreign digital companies and foreign e-commerce operators; it should be specifically clarified that the sale of goods or services facilitated through emails or non-public ERP platforms should not be subject to EL. Further, a clarification to specifically exclude intra-group transactions from the scope of EL should be provided.

5. Simplify Compliance

The newly inserted provisions of tax deduction at source under section 194-Q and tax collection at source under section 206C(IH) entails serious compliance for the taxpayers. Neither TCS on sale of goods nor TDS on purchase of goods appears to be a revenue collection exercise since the TCS/TDS rate is kept very low at 0.1%. Hence, it appears to be information collection exercise for Government. Contrary to intent of deepening and widening the tax net, the compliance burden and impact of TDS/TCS falls on those taxpayers who are already within the tax net.

It is recommended that the provision be withdrawn completely for transactions which are already within the GST regime and/or B2B transactions. The provisions be made applicable only to payees or payers who are not registered with GST. This will then align with the Government’s intention of widening and deepening the tax net.

The issues and recommendations in detail regarding the above has been set out in the memorandum.

6. Provide Stability in Tax Policies

It has been observed that sudden change in policies has created uncertainty and severely impacted large investments. For example, the entire viability of a project could depend on the duty arbitrage to encourage manufacturing in India versus imports into India. It is very important to have a commitment from the Government regarding stability in the tax policy announced by the Government for a definite period. It is recommended that a mechanism should be developed under the tax laws to ensure stability, consistency and predictability in the tax regime. This will indeed provide impetus to fresh investments and would pave a way for fair tax regime.

We, at FICCI, would be delighted to work with the Government to provide all possible support in this regard.

ECONOMIC OVERVIEW

State of Economy

The global outbreak of Covid-19 pandemic in early 2020 was of unprecedented stature. While the health repercussions were an obvious effect, the virulent nature of the infection and the consequent lockdowns had a serious economic fallout. The twin crises - both on health and economic front - have been a test of resilience and grit for countries across the world including India.

Earlier this year, at the time of announcement of the Union Budget 2021-22, things seemed to be settling down for India with signs of recovery becoming evident. The Budget 2021-22 announcements were aligned with the government's broader vision of creating a self-reliant India. And the proposals carried forward the balanced approach of the government with focus on reviving the economy.

But in no time the country was struck by the devastating second wave of the pandemic. The second shock of the pandemic was much more damaging on the health front than the first wave, and it did cause a set back to the nascent economic recovery. However, according to estimates by Reserve Bank of India, the loss of output because of the second wave was about 40 percent less than during the first wave.

With two waves of pandemic behind us, the past eighteen months have been unconventional and unsettling on many counts. Even as we continue our fight against the pandemic, the economy has once again set on the recovery course – which is gradually gaining momentum and strength.

After posting a y-o-y contraction of 7.3 percent in GDP growth in the year 2020-21, the latest numbers reported a double-digit y-o-y growth of 20.1 percent in quarter 1 of 2021-22. This growth though has come on a low base, but it reflects a recovery of more than 90 per cent of the pre-pandemic Q1 output of 2019-20.

The performance of agriculture sector was robust throughout the pandemic period. In fact, agriculture was the only sector to post growth in the previous financial year. Furthermore, the growth expectations of the agriculture sector remain buoyant for this fiscal as well. The farmers have been able to cover the lag in kharif sowing as monsoon showers picked up pace in September 2021 after an extremely dry spell in the prior month.

The industrial activity is also gaining traction, which is reflected in a broad-based pick up in lead indicators. Moreover, the swift pace of vaccination is lending momentum to the contact-based services as well.

The index of industrial production, which is one of the key gauges of industrial activity in India, has recovered to be at pre-pandemic levels. The overall industrial production index number for the month of August 2021 has reported a growth of 3.9 percent over the same month of 2019.

On a cumulative basis, the overall index has posted a growth of 28.5 percent over the period April-August 2021 on an annualized basis, vis-à-vis a 25.0 percent decline noted last year.

High frequency indicators such as power consumption, rail freight, e-way bills, GST collections, highway toll collections, air freight/ passenger traffic, all signal towards economic engine moving once again.

The vaccination drive, a sustained drop in new Covid cases and improved mobility over the past few months have brightened the economic prospects. However, what we are seeing is a K-shaped recovery. Be it the performance of key macro parameters, the urban rural dichotomy or the multi speed recovery of sectors – what is emerging is a picture of many contrasts. The pandemic has accentuated some of gaps and inequities existing in our present economic system.

While on one hand, foreign trade, electricity generation, tax collections have all been buoyant so far in this fiscal year and the concerns on inflation front have also receded for now, on the other hand, a note of caution continues to be in place as far private investments, employment generation is concerned. Investments are not yet strong, and some degree of tentativeness remains in the demand recovery. Consumption demand must improve ahead of investment demand for a sustained upswing to take hold.

Furthermore, even though both the demand and the supply sides seem to be catching pace, a significant gap remains. The demand pulse is noting an uptick. With a wider vaccination coverage and onset of festive season, the pent-up demand is driving consumption. Reserve Bank of India's latest Consumer Confidence Survey has also reported an improvement in consumer confidence index to 57.5 in September from 48.6 in July. Consumer confidence for the year ahead period has noted an improvement as well. The future expectations index moved to 107 in September from 104 in July. However, thus far the private final consumption expenditure is below (by about 12 percent) the pre-pandemic level.

Besides, despite things easing on the supply side, recent global developments on the energy front/shortage of industrial inputs can seriously challenge manufacturing activity going forward. These persisting uncertainties are also reflected in the capacity utilization rates which are yet to return to pre-Covid times. The private investors continue to remain on the fence as far as their intentions on new investments are concerned. In fact, at present the existing capacity seems enough to absorb a further increase in demand. It may also be noted that ideally a capacity utilization rate of 78-80% triggers higher investment and growth cycle. Only larger firms in the in core segments like steel, cement, non-ferrous metals have not only been able to deleverage but also crossed the threshold for investment trigger. These have started brownfield investments. The smaller units are not in a position to do that. So, the green shoots of recovery in private sector are unevenly spread.

Moreover, on the global front, the divergences in the recovery being witnessed by advanced and emerging economies are also becoming wider. According to IMF's latest World Economic Outlook, the global economy is projected to clock a growth of 5.9 percent in 2021 and 4.9 percent in 2022. The impact of the spread of the delta variant and persisting supply side constraints have moderated recovery in some advanced nations. Also, vaccine access remains a major policy challenge. According to the IMF, the risks are tilted to the downside as the possibility of more virulent variants of COVID-19 spreading remains real and this can happen before the outreach of the vaccine is expanded.

Amid this, India’s focus on vaccination-based strategy to manage the crisis has helped alleviate stress to some extent. The progress made on vaccination front is encouraging. Average daily vaccination rate has increased to 78.10 lakh doses per day in September 2021 from 2.35 lakh doses per day in January 2021. As on October 12, 2021, 96 crore doses have been administered – covering 70 percent of the adult population.

Furthermore, various measures announced by the Government over the last few months have provided some relief, especially the extended coverage of ECLGS scheme, and support to tourism and healthcare sector. These measures have been timely, and their seamless implementation should help us prepare better to face the subsequent waves of the pandemic.

The recent amendment of taxation laws to do away with retrospective tax provisions is a welcome move by the government. This will strengthen India’s credentials as a key investment destination. Tax rates too have been brought down and there is a clear focus on improving ease of doing business. These measures are well intended to make India a competitive, transparent and a profitable investment destination.

The Production Linked Incentive (PLI) scheme is also attracting international attention. The sectors covered under the PLI scheme are strategic, technology intensive and also important from the perspective of employment generation in the country. Indian economy offers huge opportunity for these sectors not just from the domestic market perspective but also to make India an export hub for these products.

The time is ripe to continue the momentum. Given the experience over the past year and a half, we need to be in a state of preparedness to meet any adversity on the health and economic front. FICCI hopes that in the Union Budget 2022-23 the government will continue to address the challenges and take concrete steps towards bridging the existing gaps that are in line with new realities. **In this context, FICCI would like to make the following suggestions.**

Short-Term Measures

1) Ramping up vaccination program across the country

India’s economic recovery is closely related to the speed and progress of our vaccination program. We have done well over the last few months in terms of administration of vaccines. It is important that the momentum is maintained and government plans for vaccination of children as well as offering booster shots particularly to the vulnerable sections. Necessary funds should be allocated in the upcoming budget for this purpose.

2) Improving the scale of genome sequencing for covid-19

The policy response to future Covid waves should be based on science. Our approach needs to become more pro-active. Genome sequencing of the virus is important to understand the dynamics of virus mutation. The Indian SARS-COV-2 Genomics Consortium (INSACOG) of 10 research labs that was set up in Dec 2020, has been doing work in this area. However, there is a scope for improving it further as the level of genome sequencing has remained low.

There is a need for systematic and large-scale data collation on a Central Platform. A National network can be set up in all States to facilitate the collection and collation of requisite data. A robust genomic sequencing network across cities is crucial to inform vaccine development for subsequent waves. Similarly, studies on vaccine efficacy and the period of immunisation need to be undertaken so that we can plan for the next stage of vaccination.

3) Upgrading nation-wide healthcare infrastructure

Government has already envisaged increasing public spend on healthcare to 2.5% of GDP (from around 1.3% currently). We urge the Government to start spending an extra 0.5% of GDP every year on health for the next five years.

To strengthen health infrastructure in the private sector, government should consider offering weighted deduction to healthcare providers for capex incurred for fighting the covid pandemic and for expenses incurred on skills development in the healthcare sector. Further, government should launch a Health Infrastructure Fund and a Medical Innovation Fund to facilitate greater access to capital for industry.

4) Providing relief to the urban poor through Urban MNREGA

Covid-19 has caused immense stress amongst the poor, both in rural as well as urban areas. Unemployment rate across India has remained significantly higher in urban areas as compared to the rural areas. During the covid-19 phase, while the rural sector has displayed resilience, urban sector has taken a severe hit. The monthly unemployment statistics by CMIE reveal that the unemployment rate had touched a peak level of 14.7% in urban areas in May 2021, though it has come down since then (to 8.6% in September 2021). In rural areas the unemployment rate stood at 6.1% in September 2021. Even though the economic activity indicators are showing signs of revival, the poor remain under stress, with lack of employment opportunities. A continuous support to them will help in boosting overall demand. Currently, the consumer sentiment is still low when compared to the pre-covid levels, especially in the urban areas.

For the urban poor, MGNREGA can be replicated, and government may consider offering work to people for carrying out sanitation activities, planting trees, cleaning and upkeep of common areas etc. They can also be used for building residential houses for the migrant workforce.

5) Offering interest subsidy on housing

The housing and real estate sector can be a force multiplier for growth and the need of the hour is to offer credit at extremely low rates of interest for the next few years. Construction sector can play a vital role in economic recovery and employment generation - It is one of the most employment intensive sectors. Housing sector has tremendous forward and backward linkages and must be promoted at the current juncture. Growth in the housing sector has an impact on 200 sectors. There can be a targeted intervention by the government by way of offering an interest subsidy of 3-4% on housing loans for a period of

3-4 years. This will give a boost to housing sales and will lead to no leakages as it will be a targeted measure.

6) Extending further support to MSMEs

MSME sector has faced immense stress due to two consecutive covid-19 waves. Even in pre-covid times, MSMEs faced challenges in meeting their financial requirements, especially for working capital. The situation worsened due to the pandemic. As per TransUnion report, the number of MSME entities with clean payment record has significantly reduced post-COVID wave 1. In the post covid period, i.e. January to March 2021, nearly 80% of the MSMEs have missed at least one or more payments due, as against 55% one year back during pre-covid times. Any possible third covid wave could further aggravate the stress in this sector. In light of this following may be considered:

Change in Classification Norms of MSMEs for NPAs: It is recommended that the 90 days limit fixed by RBI for classifying overdue of MSMEs should be increased to 180 days so that MSMEs are not constrained to divert their working capital towards servicing of their loan-instalments and clearing of their over dues at the cost of normal business operations. This improvement in the RBI guidelines will save a large number of MSMEs from turning sick or getting closed resulting in loss of economic activity and employment.

Personal Guarantee Requirement: MSMEs are often asked to provide personal guarantee to the banks for taking a business loan. These units generally use all their resources to set up a business which helps in building the country's economy. Asking for additional personal guarantee creates a barrier for them to grow or sustain hence it is suggested that RBI and Government should fix a threshold limit as per the categories of Micro, Small and Medium till which no or minimum percentage of personal guarantee is asked for a business loan.

Automatic Publishing of GST registered MSMEs' invoices on TReDS: The TReDS initiative by the Government is a wonderful tool for MSMEs to access the immediate fund at ease. Currently it is mandatory for all CPSEs and companies having annual turnover of more than Rs. 500 Cr. to register on TReDS platform. It is suggested that the registration should be mandatory for all companies having the turnover of more than Rs. 250 Cr. as it would increase the purview of TReDS.

Further, every tax invoice raised by GST registered MSME unit should reflect automatically on the respective TReDS platform where MSME unit is registered. After the delivery of Services or Goods, within a certain number of days, the corporate must accept or reject the automatically published MSME's invoice. After that period, the published MSME's tax invoice should be deemed accepted and should be available for banks to provide fund to MSMEs.

Enhance loan limit under CGTMSE: Collateral free loans under CGTMSE, either term loan or WC loan should be increased from existing Rs. 2 crores to up to Rs. 5 crores to MSMEs, irrespective of their constitution (Private Ltd, LLP, Partnership and/or proprietorship) provided all other criteria are fulfilled.

7) Supporting Non-Banking Finance Companies

Besides banks, NBFCs are widely acknowledged as an important source of organised credit to MSME sector. However, current share of organised sector in MSME credit is less than 20%. NBFCs can play a vital role in increasing the organised sector contribution to MSME credit.

The multiple stimulus packages announced by the RBI and Ministry of Finance have given an interim relief to non-bank lenders. However, since many of these measures require Banks as intermediaries, the liquidity transmission has not been effective. This is primarily due to the adverse risk perception towards non-bank lending sector. As a result, whilst NBFCs continue to face liquidity issues, the Indian banking system is flushed with liquidity.

Non-bank lenders have higher exposure to the MSME and infrastructure sectors which are most impacted by Covid-19 related stress. Thus, they will continue to face liquidity challenges in the absence of any specific liquidity support.

The government may consider a separate direct line of credit for non-bank lenders at a pre-fixed rate having regards to tenor and rating of the borrower. This will enable NBFCs/HFCs to raise funds to refinance the maturing debt and manage ALM.

8) Expanding the scope of loans given under PSL to agriculture sector / farmers

Under the Priority Sector Lending guidelines, for agriculture a target of 18% of adjusted net bank credit has been set. A large proportion of agri-loans (nearly two-third) is skewed towards short term loans of upto 6 months. There is a need to improve the share of medium to long term loans in the agriculture sector – loans for farm equipment, cold chain, common agri-infrastructure, warehousing etc.

Crop loans to farmers are given for a single season and on return of the outstanding loan amount the next credit cycle begins. We need to work out measures for offering crop loans to farmers for the full year – both Kharif and Rabi season. This can be supported by developing farm gate infrastructure and promoting warehouse receipt financing.

Many agri-tech start-ups are working and offering solutions that provide blockchain based warehousing so that no frauds can take place. These companies are working to create warehouses near farms so that farmers can get a decent time window to dispose of their produce. There are other agri-tech firms that offer solutions to farmers for reducing the usage of fertilisers, improve water efficiency and economise the use of other agri-inputs such as seeds. It is therefore requested to consider including loans extended to such Agri-tech companies as part of the Priority Sector Lending under Agriculture. Further, as these technology services need to be paid for by farmers, crop loans offered by banks to farmers could include subsidized loans for payment of such services.

In context of agriculture, another suggestion is to incentive seed dealers, fertilizer dealers and suppliers of other agri-inputs and tools to set up digital payments acceptance infrastructure. This will promote usage of the RuPay Kisan Credit Cards and loans to farmers can be released through the credit cards for buying farm supplies. This will also prevent the misuse of the farm loans.

9) Encouraging loans for social infrastructure projects related to sanitation

Under Priority Sector Lending (PSL) norms for Social Infrastructure, waste management activities – particularly faecal sludge management – should be included. Under the Swachh Bharat Mission, while lakhs of toilets have been set up across the country, maintenance of the same is a key issue. Banks must make available financing for companies involved in these activities. PSL should be extended to commercially viable technologies in the area of waste management as well as to projects that lead to transformation of waste to energy. Some of the municipal corporations in the country such as Indore and Nagpur have successfully implemented such projects.

10) Managing inflation: Reigning in fuel prices by unwinding taxes

Fuel prices are at an unsustainable level. Crude oil prices have averaged $70.8 per barrel in first half of this fiscal compared with $37.1 per barrel in the same period last year. Plus there is a major component of taxes built into the end price. This is a serious concern as fuel prices are putting a massive burden on consumers – the middle class – and limiting industrial recovery. There has been too much of cost passed on to the economy. Government may consider unwinding some taxes. It could also bring them quickly into GST. Otherwise, the risk of inflation spiral going up is high.

11) Offering regular subsidy to PMUY beneficiaries for incentivising cooking gas usage

India's cooking gas prices have seen a secular uptrend since late 2020, increasing from an average of INR 720 for a 14.2kg cylinder in 2019 to INR 870/cylinder by August 2021. This is likely to rise by another 15% to INR 1,000/cylinder following the latest increase in natural gas prices. While this will hurt the 290mn households who use cooking gas, the impact will be more acute for the 80mn users who belong to the vulnerable section of society.

These 80mn users (likely to increase to 90mn over next few quarters) are beneficiaries under government's Pradhan Mantri Ujjwala Yojana (PMUY) scheme and primarily include women members of BPL (Below Poverty Line) households and seven other categories (SC/ST, PMAY, AAY, Most backward classes, tea garden workers, forest dwellers, islands). The scheme was launched in 2016 to encourage households to reduce their dependency on fuel such as kerosene and firewood that have a more detrimental impact on health and climate. The subsidy component under the scheme has focused more on providing new gas connections, free first refills, free hotplates, etc., rather than regular subsidies on every refill. However, to aid lower income households during the first wave of the COVID-19 pandemic, three free cylinder refills were offered to PMUY recipients, at a total cost of INR 81.62bn in FY21.

With recent increase in prices, affordability has become a major challenge for such households for using cooking gas. In fact a recent study conducted by Council on Energy, Environment and Water (CEEW) points out that 84% of households that use traditional solid fuels along with LPG cite high cylinder costs as one of their reasons for stacking fuels. Similar finding was reported back in 2016 by Ministry of Petroleum Planning and Analysis (PPAC) survey ahead of the launch of the scheme. CEEW also found that a typical rural Indian household would have had to spend 6.7% of its total monthly expenditure on LPG to use it

as an exclusive cooking fuel (at a subsidised LPG refill price of Rs 580 in 2020). This is around 40% higher than what rural households actually spent on cooking fuel at that time (4.9% of the total monthly expenses).

Given the affordability issue, if the government partially subsidises the usage of 6-7 cylinders annually to PMUY beneficiaries (say price in excess of INR 500/ cylinder to be borne by the government), the fiscal cost is likely to be small. For instance, if existing price is INR 1000/ cylinder, the subsidy burden will not exceed INR 300bn per year (0.14% of GDP).

12) Incentivising Research & Innovation

If India has to remain relevant in this era of globalisation, it is clear that cutting-edge R&D is crucial and the current pandemic has only reiterated this. Our presence in the global market is also determined by our indigenous R&D efforts. India's R&D spending is quite low at 0.67 % of GDP, vis-à-vis countries like Korea (4.92% of GDP), Japan (3.14%of GDP), Germany (2.94% of GDP) that spend substantial amount on R&D. India needs to enhance public spend on Research and Innovation from the current 0.67% to at least 1.5% of GDP.

Indigenous R&D must be supported through fiscal incentives and by having a robust innovation ecosystem. While in the new corporate tax regime, all deductions and exemptions have been phased out, investment in R&D must be given differential treatment as this is a key source for innovation and growth.

Long-Term Measures

1) Improving logistics

Infrastructure bottlenecks continue to adversely impact the cost of doing business in India, hurts competitiveness and makes it difficult to achieve the objectives of 'Make in India'. Logistics costs in India is around 14 per cent of GDP as against 8-10 per cent for other developed economies.

On improving logistics, our suggestion is to fast-track the projects linking industrial parks with different modes of transportation – railways, roads, ports, airports. The government could perhaps announce 10 industrial parks where such connectivity will be completed in a time bound manner.

2) Leveraging Blue Economy

Blue-Economy (Marine Economy) is the next big opportunity for India's economic growth. The Blue economy is currently about 3-4% of our GDP with budgetary allocation of about Rs 53000 Cr. Blue Economy's multifarious opportunities warrant a separate Ministry/ Department for inter-ministerial & States' coordination. The department would enable harnessing greater benefits of Blue Economy, with almost 7500 Km of coastline that India enjoys. Sagar mala project itself could be the next big economic corridor if synergies on coastal shipping, cruise tourism, inland waterways, fisheries development, off-shore clean energy, deep sea mining for rare-earths etc. can be brought under ambit of a central Ministry/Department for coordinated growth of the sector.

The concept is new to industry and needs to be showcased in a big way for the next few years. Global best practices can be easily imbibed once they have knowledge & exposure of this opportunity.

3) Investing in digital infrastructure

The Covid-19 pandemic has sparked a sudden shift in economic activity from physical to digital and has transformed peoples' approach towards work and mobility. The current crisis has underlined the criticality of digital infrastructure across different sectors- be it healthcare, education, retail, entertainment, large enterprises, small companies, start-ups etc.

In order to meet the growing digital demand, it has become imperative to offer high quality of service with superior connectivity and data speed. Moreover, there is a need to bridge the disparities in access to digital means that exist at various levels in India (Urban-Rural Divide, Regional Divide, Digital Gender Divide).

Investment in digital infrastructure has been much lower in India than in most large economies. Large economies such as the US, Japan, Germany, the UK spend 1%-1.5% of their GDP for building digital Infrastructure. In contrast, India, with a much larger population, has been spending only 0.5% of its GDP on digital infrastructure. We should be aiming for a much higher upfront investment on digital infrastructure. Both private sector and government will have to share the responsibility of channelizing this investment. The following models may be considered for the same:

Option 1: A PPP model. Mirroring the NHAI model, using partly private sector funding, initiative, and management capacity, leveraging their capability to bring efficiencies and implementation best practices. The Government is exploring this model in BharatNet III.

Option 2: A "wholesale entity" model, which draws on the structure and key features from the UK infrastructure model of the Entity Openreach. The entity itself could comprise of the central and state governments as well as private telecom players, ISPs and other stakeholders from the education, health, industry 4.0, agriculture, and other sectors. In this option, the ownership would remain with the government to make sure that the vision is intact and appropriate control is exercised. Revenue would be realized from leasing out fiber to private players and from utility applications. Government will also have a deeper say on the detailed architecture, which will ensure fiber is leasable to private players to earn revenue and the last mile service delivery is assured in rural areas at standards on par with cities. Once the operational model is finalised and we are at the deployment stage, India should institutionalise a Network Readiness Index to track and measure the performance on digital infrastructure creation and impact to drive the $5 trillion vision as metric.

4) Launching concept of Innovation City

New innovation and technology hubs are emerging around the world outside of traditional hubs like Silicon Valley. With technology advancements like cloud computing, companies can rely on talent located elsewhere. Today, India has been able to successfully position itself as a promising start up hub.

India has the capability and the capacity to attract and support not only home-grown start-ups but global start-ups as well to innovate and subsequently scale across the world. The timing is apt to give wings to an Indian Innovation City – which will be an aspirational yet affordable destination for young entrepreneurs to bring their ideas to life.

Mysuru in Karnataka, GIFT City in Ahmedabad, Gurugram in Haryana, Noida in Uttar Pradesh, Kochi in Kerala can be among the first contenders for the Start-up Nirman Hubs.

To begin with the government can allocate a suitable piece of land for the Innovation City and establish a "Single Window Approval" for clearances/permits for start-ups as well as companies/institutions setting up supporting infrastructure. Direct & Indirect Tax benefits in addition to establishment of tax holidays for initial establishment period, differential fiscal incentive structure depending on industry type (manufacturing/services), and performance linked incentives to reward successful entrepreneurs will also provide effective support.

5) Promoting development of Green Technologies across sectors

Hon'ble PM has played a leadership role at the global level in giving a push to renewables, waste management etc. To further give impetus to realizing his vision, it is important to lay down policy for green technology. Govt must create a facilitating environment for green technology. China incentivized companies in developing green technology in solar etc. by providing free land, concessional power cost and funding at low interest cost. Many other countries which have emerged as hubs of solar modules, components etc like Taiwan, Malaysia, Vietnam did so on back of huge government incentives. In order to compete with these countries, government needs to come up with similar incentive framework to promote local development of green technologies across sectors.

6) The budget should aim for a credible medium term fiscal consolidation glide path. The focus should be on faster normalisation/reduction of revenue deficit than fiscal deficit. This would allow for greater spending on investments by the government, which is critically needed to make a success out of the ambitious infrastructure plan (National Infrastructure Pipeline). The higher spending on infrastructure will raise the growth potential and crowd in private investments.

DIRECT TAX

Section I

Ambiguities prevailing under Concessional Tax Regime for Companies and Key Issues Related to Amendments made by the Finance Act, 2021

1.1 Extend Cut Off Date for Commencing Manufacturing Operations under concessional tax regime of section 115BAB of the Act from March 31, 2023 to March 31, 2025

Issue

As per Section 115BAB of the Act, a domestic company engaged in the business of manufacturing and production of prescribed articles or things or engaged in distribution thereof, has an option to pay tax at effective rate @ 16.17% subject to fulfillment of prescribed conditions. One such condition is that the Company should commence manufacturing/ production on or before March 31, 2023.

The Government has introduced this section with the intent to boost the economic growth in the country. The manufacturing sector growth is vital for GDP growth; hence this beneficial tax regime is introduced to encourage corporates to open more manufacturing facilities to develop India as an alternative manufacturing base to China.

However, in the wake of ongoing COVID pandemic, the economic activity has been adversely affected with supply chain disruptions, labour mobility, spending slowdowns, jitters over credit markets etc.

Amid all this, the newly established domestic companies are unable to work towards meeting the projected timelines and it looks difficult to meet the March 31, 2023 deadline for commencing manufacturing operations – more particularly for heavy industries with long gestation period. Prior announcement of extended date will facilitate global players to commit capital to India to set up new manufacturing facilities in a planned and organized manner.

Recommendation

It is suggested to extend the cut-off date for commencing of manufacturing operations under section 115BAB of the Act to March 31, 2025, from March 31, 2023.

Other Issues - Companies opting for concessional tax regime – Section 115BAA and Section 115BAB

- The Government had promulgated The Taxation Laws Amendment Ordinance, 2019 (hereinafter referred to as 'the Ordinance'), amending the provisions of the Income-tax Act, 1961 and the Finance (No. 2) Act, 2019 which was subsequently legislatively ratified through an Amendment Act. The government has given an option to companies to migrate to a very competitive tax rate structure under section 115BAA of 25.17% (inclusive of applicable surcharge and education cess). The provisions of MAT shall not be applicable to companies opting for the concessional tax regime under section 115BAA of the Act.

Further, 115BAB of the Act has been inserted to provide an option to the domestic companies engaged into manufacturing activities, incorporated on or after 1st October, 2019 to pay income tax at the rate of 15% (17.16% inclusive of applicable surcharge and cess).

Also, domestic companies availing such an option -

- Shall not be allowed to avail any incentive/exemption offered under the Act including additional depreciation.
- Shall not be allowed to set off any loss carried forward from earlier year, if such loss is attributable to any of the exemption/incentives including additional depreciation.
- Once such option has been exercised by any Company, there is no option to opt out of the concessional income tax rate.

Some of the key issues and recommendations pertaining to concessional tax regime for companies are enclosed below**:-**

(a) Allow MAT credit for companies availing beneficial rate of tax under section 115BAA

The companies opting for beneficial rate of tax under section 115BAA are not permitted to carry forward and utilize their MAT credit in case the option is exercised.

Issue

MAT credit is nothing, but excess tax paid over normal income in the preceding years. Hence, it is nothing, but in the nature of advance tax paid by a Company. Thus, disallowing the companies to utilize their MAT credit merely because they opted for a beneficial provision of the Act does not seem to be in line with the Government's intention of providing a competitive edge to Indian corporates.

The utilization or not of MAT credit will significantly impact the financial and cash flow positions of companies. Keeping this in mind appropriate amendments ought to be made in the Act.

Recommendation

The Act should be amended to allow utilization of MAT credit even for companies exercising option under section 115BAA of the Act since the same is at par with advance tax and TDS.

(b) Provide Clarity for exercising option under section 115BAA of the Act in case of noncompliance of conditions stipulated in section 115BAB of the Act

First proviso to sub-section (5) of section 115BAA of the Act states that in case of a person whose option exercised under section 115BAB of the Act has been rendered invalid due to violation of specified conditions, such a person may exercise the option under section 115BAA of the Act.

However, sub-section (7) of section 115BAB of the Act mandatorily requires the option to be exercised in the prescribed form on or before the due date of filing the first return of income.

Similarly, section 115BAA(5) of the Act also requires the option to be exercised on or before the due date of filing the return of income in the prescribed form. The proviso to section 115BAA(5) clarifies that a person whose option under section 115BAB of the Act has been invalidated on account of non-fulfilment of certain conditions may exercise option under section 115BAA of the Act but there is no clarity how this option can be exercised if the option under section 115BAB is denied at assessment stage by the tax officer.

Issue

- Considering that practically since the option of exercising the option under both the sections would have been undertaken before the due date of filing the return of income, it may not be possible to shift from section 115BAB to section 115BAA and hence the need of a clarification in this regard.

Recommendation

- A clarification may be issued that even though option for exercising option under section 115BAA of the Act was not exercised in the prescribed form on or before the due date of filing the return of income, the same can be subsequently claimed if conditions stipulated in section 115BAB are not met.
- Alternatively, a company exercising option under section 115BAB may also be permitted to opt for section 115BAA to enable the benefit of either of the provisions as long as the conditions are fulfilled.

(c) Restriction on "use" of any plant or machinery previously used for any purpose in Section 115BAB of the Act – Shift of emphasis from "transfer" to "use" can have enormous consequences

Issues

- As per one of the conditions imposed in section 115BAB of the Act, the company should not "use" any plant or machinery previously used for any purpose. The new provision uses the language of "use" instead of "transfer" to new business of machinery or plant previously used for any purpose as used in several existing incentive provisions of the Act such as sections 10AA, 80IA, 80IB, 80IC of the Act.
- Shift of emphasis from the word 'transfer' to "use" in section 115BAB of the Act results in unintended limitations and irritants in business appraisal of the company in various scenarios.
- Restriction w.r.to 'use' of second-hand asset would unintendedly apply to cases of asset being taken on hire even if it is for a very short-term period such as electric generators, etc., assets received under bonafide business reorganisation, cases where part of the manufacturing is outsourced to a third party on job work basis, etc.

Recommendation

- It is recommended to place condition of second-hand plant and machinery along the lines of other incentive provisions under the Act which has been tested over time

instead of introducing some new ambiguous language which shall result in new interpretational issues and unintended consequences.

(d) Explanation to section 115BAB(2)(b) clarifying that certain activities shall not be considered as manufacture or production of any article or thing should be omitted

Issue

- Newly inserted section 115BAB of the Act provides for concessional tax rate of 15% in case of newly incorporated domestic companies subject to fulfilment of certain specified conditions which are:-
  - The company is incorporated on or after October 1, 2019;
  - Has commenced manufacturing on or before March 31, 2023;
  - Not engaged in any business other than manufacture or production of article or thing and research relating to those article or thing;
  - Is not formed by splitting up or reconstruction of a business already in existence.
  - Does not use any machinery or plant previously used in India for any purpose.

  In this regard, Explanation added to section 115BAB(2)(b) of the Act clarifies that certain activities like software development, mining, gas bottling, printing of books, production of cinematograph films, etc. shall not be regarded as business of manufacture or production any article or thing.

  It seems the Explanation is inserted to nullify various Supreme Court rulings which have upheld that the said activities constitute manufacture or production of article or thing for granting certain tax incentives.

  It is submitted that each of the activities referred in the Explanation require significant capital investment in new plant & machinery and creates jobs in the economy which is the object and purpose of granting concessional rate of tax of 15% under section 115BAB of the Act. The provision does not grant benefit for service sector like telecom, retail, e-commerce despite the fact that significant investment is required even in such industries. Considering the exclusion for service sector, it is highly unfair to artificially restrict the benefit to those industries which have judicially been held to qualify as manufacture or production of article or thing.

Recommendation

- Explanation to section 115BAB(2)(b) of the Act denying the benefit of 15% rate of tax to certain sectors which have judicially held to constitute manufacture of article or thing should be omitted to allow the section to have its full effect and encourage fresh investment and jobs in the economy.

(e) Allow adding back unabsorbed depreciation to written down value of block of assets

Proviso to sub-section (3) of section 115BAA allows companies to add back unabsorbed depreciation as on April 1, 2020 to the written down value of the block of assets. However, the benefit is only permitted to companies exercising the option in AY 2020-21.

The concessional tax regime was introduced to provide a level playing field to domestic companies and give them a competitive edge. Not allowing the companies to write back their unabsorbed depreciation takes away the extra benefit granted to companies who choose to exercise the option in AY 2020-21 itself.

It is requested to extend the benefit of adding back unabsorbed depreciation to written down value of block of assets for companies exercising the option at any given point of time.

1.2 Allow depreciation of goodwill in respect of for transactions completed prior to 1 April 2021 and for purchased goodwill in non-tax neutral transactions

Issue

- The Finance Act 2021 made far reaching amendment of denying depreciation on goodwill, an issue which was in a way settled by the Supreme Court in the favour of the taxpayers. It is significant to note that while in legal form, the amendment was stated to be prospective i.e. it took effect from 1 April 2021 and applied from A.Y. 2021-22 onwards. However, in substance, the denial of depreciation has a retrospective impact on past business transactions and is contrary to the professed policy of current Government of not making retrospective amendments prejudicial to the taxpayers.
- The amendment has far reaching adverse impact on industry and businesses which had so far arranged their affairs on the basis that goodwill will be allowed depreciation for tax purposes – at least for acquisition in non-tax neutral transaction. The pricing of the deals, fair exchange ratio between shares of amalgamating/demerged and amalgamated/resulting companies, indemnities provided by sellers, etc. were all based on admissibility of tax depreciation on goodwill in the hands of the buyer – at least on purchased goodwill.
- The Explanatory Memorandum to the Finance Bill, 2021 itself acknowledges that there is 'valid claim' of depreciation on purchased goodwill in view of Smifs ratio.

Recommendation

- There is a strong case to at least make the amendment on prospective basis such that depreciation is denied only to goodwill acquired on or after 1 April 2021 and goodwill acquired in past (whether in tax neutral or taxable transaction) is 'grandfathered'.
- Without prejudice, the denial of depreciation on goodwill acquired in taxable transaction needs reconsideration. The seller is liable to pay capital gains tax on such transaction. The value of goodwill in such transaction indicates consideration paid by the acquirer to secure synergy, larger market share, better cash flow, forward or backward integration, competitive strength, and higher efficiency in existing business, which leads to better profitability and higher tax. Hence, claim of depreciation on goodwill should not be

denied for acquisition of business in non-tax neutral business reorganization like slump sale/exchange or itemized sale.

1.3 Issues related to Equalisation Levy

Background

- The Equalization Levy ("EL") was first introduced in India in 2016 and was limited to online advertising revenue earned in India by a non-resident. However, in 2020, the scope of EL was expanded w.e.f. 1 April 2020 to cover "e-commerce supply or services" provided or facilitated by a non-resident 'E-commerce Operator'.
- Further, Finance Act 2021 expanded the scope of EL charge to cover acceptance of offer for sale, placing/ acceptance of purchase order, payment of consideration, supply of goods/ provision of services partly or wholly.
- Moreover, even the term consideration was defined to include consideration for sale of goods or provision of services irrespective of whether the goods so sold belong to the e-commerce operator or the services are provided by the e-commerce operator or not.
- In this backdrop, following are some key recommendations in relation to EL

(a) Exclusion to be provided to payment aggregator or payment gateways (covered under RBI Guidelines) which merely facilitate the payment leg of the sale transaction and function similar to a bank

Issue

- The broad scope of EL may also cover payment aggregators or payment gateways which act as intermediary by facilitating collection and settlement of payments between customers and sellers/ service providers. The RBI Guidelines also require that the payment function should be undertaken through a separate entity as against the marketplace function. This will further reduce the visibility of payment systems over the transaction. The payment entities merely assist in completion of payment arm of the transaction and are not involved in selling of goods or services.

Recommendation

- It is recommended that the CBDT should specifically clarify that the payment aggregators and payment gateways which are governed by RBI Guidelines are not covered under the scope of EL.

(b) Clarification on person liable to EL where multiple e-commerce operators are involved in the transaction chain

Finance Act 2021 inserted an Explanation in S. 164(cb) to provide that where even a specific activity such as placement/ acceptance of purchase order, payment of consideration, any part of sale or supply etc. is carried out online, such activity constitutes an "online sale of goods" or "online provision of services" and thereby trigger EL charge.

Issues

- The digital business models are highly integrated with multiple e-commerce operators sometimes being involved in the transaction chain.
- For instance, consider business models where there is one e-commerce operator (ACo) which merely lists the products and permits placement of purchase orders thereon with respect to various other online sellers/ e-commerce operators (say BCo). In such case, on acceptance of the purchase order, the customer will be redirected to BCo's platform where the sale will be actually concluded. The customer can buy the product only on BCo's platform. Further, payment may be made using platform of payment gateway (say CCo)
- In such case, there is a concern whether all ACo, BCo and CCo will be liable to pay EL on gross transaction amount specially since this may create multiple levy on the same transaction.

Recommendations

- Appropriate clarifications or guidelines may be issued that the primary responsibility to discharge EL will be on the e-commerce operator (CCo in the above illustration) who actually collects payment from the Indian party. Since the consideration will cover facilitation fees, if any, earned by other e-commerce operators from the same transaction, the other e-commerce operators may be exempted from EL levy to avoid multiple levels of taxation on same stream of income in hands of different entities.

(c) E-commerce operator be liable for Equalisation Levy (EL) on 'E-commerce Supply or Services' only when payment is routed through such e-commerce operator

Issues

- Section 165A of Finance Act 2016 requires an e-commerce operator to pay EL on consideration received or receivable from online sale of goods or online provision of service to specified person (being an Indian resident, user of Indian IP Address or Non-resident in certain specified circumstances).
- For this purpose, consideration is defined to include consideration for sale of goods or provision of services irrespective of whether the goods so sold belong to the e-commerce operator or the services are provided by the e-commerce operator or not.
- Moreover, the scope of "online sale of goods" and "online provision of service" have been expanded vide Finance Act 2021 to include acceptance of offer for sale, placing/ acceptance of purchase order, payment of consideration, supply of goods/ provision of services partly or wholly.
- In certain types of electronic commerce transactions, especially those falling within the expanded scope of "online sale of goods" and "online provision of service" discussed above, where the sale of goods or provision of service takes place directly between buyer and seller, the e-commerce operator does not have visibility over the transaction.

In such cases, the e-commerce operator may not be aware of the pricing of the goods, conclusion of the contract, etc.

- Also, there are numerous e-commerce models or aggregators where e-commerce operators are not contractually obliged to collect or pay the transaction amounts or at times even remain involved in conclusion of transaction. In fact, the suppliers/ service providers are required to make commission payments to such platforms.
- Bringing such transactions within the scope of EL not only creates difficulty in discharging the tax obligation in absence of payments but also adds to administrative inconvenience and working capital hurdles. It casts an unnecessary obligation on platforms who are not involved in consummation of the transaction between buyer and the seller.
- Even GST law also imposes a Tax Collected at Source ('TCS') of 1% on e-commerce operators from the consideration received by it on behalf of a supplier of goods or services through its online platform. In other words, there is no GST TCS obligation where the sale consideration is not routed through the e-commerce operator.
- The difficulty is highlighted by recent interim order dated 25 August 2021 passed by Calcutta HC in the case of MJunction Services Ltd. and Anr. v/s Union of India and Ors.1 in context of s.194-O which provides for TDS on e-commerce transactions of resident e-commerce participants. The HC has directed CBDT to decide upon representation filed by M-Junction on similar difficulty faced by e-commerce operator for deducting tax where payments are not routed through e-commerce operator.

Recommendations

- Appropriate clarifications or guidelines may be issued to clarify that where the transactions which are strictly between the end-user/customer and suppliers/ service providers and where no payment is ever due from the e-commerce operator to the suppliers/ service providers, EL liability in such cases will be restricted only to facilitation fee received by the e-commerce operator (if any).

  Further, if necessary, the EL law may be amended to make the NR sellers/service providers liable to EL in such cases and a reporting mechanism may be built into the EL provisions wherein such e-commerce operator will be required to provide details of the buyer, supplier/service provider, amount of consideration and other information (to the extent available with him) to ensure the transactions are adequately captured in the Indian tax net.

(d) Appeal mechanism

Issue

- The provisions prescribe an appeal mechanism only against penalty imposed and there is no appeal mechanism prescribed for the charge of EL.

[1] Order Sheet; WPO/441/2021

Recommendation

- A time bound appeal mechanism to resolve disputes in regard to the applicability and quantum of EL to be introduced which will provide for certainty and efficiencies both for the taxpayers and for the tax administration.
- Lack of efficacious remedy will lead to increased uncertainty and costs involved in approaching the High Courts for relief or settlement of dispute.

The detailed representation on EL is given in **Annexure** enclosed to this Section.

1.4 TDS on purchase of goods (Section 194Q)

Issues

- Section 194Q of the Act requires the buyer while making payment to resident seller for purchase of goods having value exceeding fifty lakh rupees in the previous year to withhold taxes at the rate of 0.1%.
- Section 206C(1H) of the Act requires a seller whose turnover exceeded Rs. 10 Crores in preceding financial year and receives sale consideration towards goods of more than Rs. 50 lakhs from a buyer to collect TCS @ 0.1%. TCS under section 206C(1H) of the Act does not apply where TDS under section 194Q of the Act applies and has been deducted.
- The provision under section 194Q of the Act has resulted in additional compliance cost and burden to the industry by keeping a track of transactional level details of realisation for each sales transaction, withholding, issuance of TDS certificate, return filing etc. TDS provisions apply on accrual system whereas TCS provisions apply on collection basis. The application of these sections parallelly creates ambiguity and increases lot of compliance burden on the both the parties.
- Large MNEs may have multiple business transactions and may also have different classes of customers and may have different business models for each class of customer. Even if IT automation is implemented, however, the interplay of TDS and TCS still remains a cause of concern across businesses.
- Such provisions not only cast onerous obligation on businesses, however, it may also pave a route for litigations during faceless tax assessments if a reconciliation of TDS/ TCS credits is sought.
- There are also operational challenges w.r.t. overpayment of TDS/TCS and then related revision of TCS/TDS returns in cases of discounts, returns, bad debts, etc. This results in challenges from accounting perspective also.
- There are business transactions where a seller receives advance payments for future sale/supply of goods. Such advance received per-se cannot constitute a sales consideration, rather is in nature of an advance receipt towards future sales. Also, there can be instances where the advance is returned as the actual sale transaction doesn't take place. In such cases, if an advance receipt is considered as liable for TDS / TCS and

subsequent sale / purchase does not fructify, it results in unnecessary practical challenges w.r.t. TDS/ TCS compliances.

- Neither TCS on sale of goods nor TDS on purchase of goods appears to be a revenue collection exercise since the TCS/TDS rate is kept very low at 0.1%. Hence, it appears to be information collection exercise for Government. Contrary to intent of deepening and widening the tax net, the compliance burden and impact of TDS/TCS falls on those taxpayers who are already within the tax net.
- Like in case of TCS for sale of goods under section 206C(1H), the new TDS on purchases also does not specifically make distinction between sales made to the intermediate customers (B2B transactions) and sales made to the final customers (B2C transactions). In absence of specific exclusion for B2B transactions, the provision appears to apply for all types of sale transactions, irrespective of whether the transaction involves sales to intermediate entities/ customers or it is sale to final customers.
- Applicability of TDS or TCS provisions to B2B transactions as well may result in tax being collected at multiple levels, in turn, may lead to cash blockage at entity level. In a supply chain structure consisting of manifold entities (as is usually prevalent in the retail sector), this would result in tax being deducted or collected multiple times on the same transaction. Deduction/collection of tax at multiple entity levels increases the administrative compliance burden, transaction costs and results in cash flow trap.
- Since B2B transactions are made with multiple vendors, it is administratively burdensome to apply for lower/NIL TDS for all vendors. Further, benefit of lower/Nil TDS has not been extended to section 194Q since section 197 is not amended.
- Further, such transactions being subject to GST, there is already an audit trail available with the GST Department which can be easily leveraged by the Income tax Department through electronic sharing of data on automated basis and making use of Artificial Intelligence to mine the data to detect tax evasion. TDS and TCS on sales results in multiple levy of tax on same transaction.
- The expanded scope of TDS and TCS severely impact 'ease of doing business' in India.
- In both the provisions of TDS and TCS, the term 'goods' is not defined. It is not clear whether the definition of "goods" needs to be interpreted as per the Sale of Goods Act or the CGST Act or some other legislation as the term 'goods' is not defined under the Act.
- For instance, whether the term "goods" includes shares, securities, money/foreign currency, actionable claims etc. within its scope is not clear since there are different inclusions and exclusions within scope of 'goods' under various laws. Under GST law, items like share, securities, money, are specifically excluded from definition of goods but under the Sale of Goods Act, goods include stock and shares but exclude actionable claims.
- While the guidelines issued vide CBDT circulars to exclude transactions in securities and commodities traded on recognised stock exchanges or cleared and settled through

recognised clearing corporations from the ambit of TCS and TDS provisions was a welcome step to avoid the wide impact of this provision on stock market transactions, the question with regard to the off-market shares and securities transactions and transactions in unlisted shares and securities continues to remain and in fact has been magnified.

Recommendations

- It is recommended that the provision be withdrawn completely for transactions which are already within the GST regime and/or B2B transactions. The provisions be made applicable only to payees or payers who are not registered with GST. This will then align with the Government's intention of widening and deepening the tax net.
- Alternatively, as between TDS and TCS, only one measure i.e. TDS on purchase of goods should be retained since it is comparatively easier to implement than TCS.
- It is recommended that meaning of "goods" may be clearly defined for better clarity of applicability of this provision.
- Consequential clarification with respect to TCS/TDS reconciliation vs income/purchases or GST returns ought to be brought in to avoid future litigations/denial of credit to the assessee.
- Neither TCS on sale of goods nor TDS on purchase of goods appears to be a revenue collection exercise since the TCS/TDS rate is kept very low at 0.1%. Accordingly, it is also recommended that exemption be granted to all transactions in shares, securities, actionable claims and foreign currency since there is ambiguity on whether these items are at all included within the definition of 'goods'. Generally, these items are traded in well-regulated financial markets and there is no need for imposing TDS or TCS when the relevant information can be easily obtained from financial intermediaries.
- It is recommended that the term "goods" should be defined under section 206C and 194Q of the IT Act to specifically exclude any products governed by regulations and guidelines issued by the Reserve Bank of India or the Securities Exchange Board of India from time to time.
- The turnover limit for applicability of TCS/TDS provisions to the prescribed assessees may be increased from INR 10 Crores to INR 50 Crores.
- The transactional threshold for applicability of the said provisions should also be increased from INR 50 Lakhs to INR 10 Crores.
- Section 197 of the Act may also be amended to enable the seller to obtain lower/NIL TDS certificate.

1.5 Issues related to Faceless Scheme

Faceless Assessment Regime – Challenges Faced and Areas of Improvement

Transparency and accountability are the two cornerstones of the present government. The 'Faceless Assessment Scheme 2020' is a turning point in the history of tax administration in

India. However, the Scheme is new and at its nascent stage, it has long way to go before it establishes itself as model platform and accomplishes the objective in entirety.

The assessments now have been undertaken in a faceless manner. The taxpayers have basis their experience in the assessments that have concluded, identified areas of improvement. We seek to bring to your kind notice some of the key areas of improvement to make the Scheme more effective, robust and in line with the accepted judicial principles and one which doesn’t in any way transgress into any of the vested rights of the taxpayers. Some of the pertinent recommendations in this regard are given for consideration: -

(a) Right to Personal Hearing

The Scheme read with section 144B of the Income-tax Act, 1961 (‘the Act’), provides the mannerism and approach for conducting the faceless assessment. Where any variation in draft assessment order is proposed against the taxpayer, Section 144B allows the taxpayer to request for personal hearing. The request for personal hearing is subject to approval of the specified officers2 and further it is to be granted if such request is covered by the circumstances to be notified/prescribed. Thus, in the present Scheme the right to personal hearing is conditional and at the discretion of the specified officers. The right to personal hearing which has always being enshrined upon all the taxpayer unconditionally, now gets vitiated pursuant to the provisions for personal hearing so codified in the Scheme. The principle of opportunity of being heard is one of the fundamental rules of natural justice and the same needs to be preserved at all costs and in all circumstances.

There have been instances where the request for personal hearing made by the taxpayers has not been approved, and the orders have been passed with adjustment to the total income.

Personal hearing can play important role in explaining complex issues to the authorities. We therefore suggest and recommend that the right for personal hearing should be universally conferred upon all the taxpayer unconditionally and without any discretion. In this regard, the SOPs/ rules may be prescribed directing that request for personal hearing should be approved without any conditions or discretion.

(b) Communication of the Draft Assessment Order

Section 144B of the Act mandates preparation of draft assessment order and where any variation in draft assessment order is proposed which is prejudicial to the taxpayer, then the taxpayer is required to be served with Show Cause Notice (‘SCN’) providing an opportunity to object to such draft assessment order. However, there have been instances where taxpayers have been served with the final assessment orders without allowing the opportunity to rebut to the draft assessment order.

The department should provide strict SOPs regarding serving of draft assessment order and issue of Show cause notice and all the procedural aspects which directly or indirectly affects genuine claim of honest taxpayers and leads to unwarranted litigation.

[2] Chief Commissioner or the Director General, in charge of the Regional Faceless Assessment Centre

Further, it is recommended that the department system should conduct internal checks and balances wherein, it can be ensured that no final order is passed without issuing draft assessment order and show cause notice in applicable cases. Monitoring Unit can be set up to oversee the compliance with the provisions.

(c) Practical issues faced during proceedings

As a part of assessment proceedings, the department can call for relevant information and provide time for submission. However, under the faceless regime the process of assessment has some of its own challenges, namely

- The notice seeking for information is drafted as a standard notice, calling for huge and cumbersome data running in hundreds of pages. Due to lack of personal hearing/physical interface the taxpayer is not able to explain the inapplicability of the details sought, cumbersome nature of the details called for, etc.
- Details are required to be furnished within very short timeframe generally within three to five days.
- Limitation of 5 MB per attachment exists as on date for each annexure and maximum of 10 annexures per submission.
- Adjournment is granted without providing subsequent hearing date or granting short timeframe.
- Sometimes order is passed without considering or without much deliberation on the submissions made by the taxpayer or even before the last date of filling the reply to notice.

(d) Resolve Portal issues

In recent times, the taxpayers have faced enormous difficulties accessing features of the portal. It leads to difficulty in complying with the notices and due dates in time. This will be amplified in return filling season with multiple users accessing the portal for return filling purposes.

(e) Rectification against order passed under faceless assessment scheme

The Scheme provides for transfer of records to the jurisdictional assessing officer for rectification of mistake. Thus, it appears that the rectification application for any mistake apparent from records under section 154 of the Act needs to be submitted to the jurisdictional officer. However, there have been instances where the officers have requested that the application for rectification should also be made online with the National Faceless Assessment Centre. Hence, there is lack of clarity regarding the authority to be approached for the matters of rectification. Further, at the same time, the Faceless Penalty Scheme gives rectification rights to National Faceless Penalty Centre.

The rectification rights should be transferred to the assessment unit/review unit of National Faceless Assessment Centre or with the Jurisdictional Assessing Officer with clear mandate on the designated officer to act upon the same within the specified time.

Certain recommendations/suggestions to improve Faceless Assessment Scheme are as follows: -

- Given its early phase and envisaging a robust process to achieve the objectives of transparency, accountability and efficiency, it will be critical for the Government to ensure appropriate investment in technology and infrastructure to manage and maintain huge amount of data and documentation that will be submitted by the taxpayers;
- With increasing number of taxpayers and return filers, the functionality and capacity of the portal can be enhanced. Alternatively, two separate portals, one for return filling and another for faceless assessment should be floated.
- Generally, Annexures are bulky files containing agreements/valuation reports etc. which exceed the limit easily and there is no provision to upload zip files. Accordingly, the size limit for each individual annexure can be enhanced and attachment of zip files to be allowed. Further, the number of attachments that can be submitted along with a submission should be increased from existing 10 to at least 25.
- Appropriate guidelines should be issued on the procedural aspects of faceless assessment scheme to the taxpayers to avoid ambiguities;
- In addition to SOPs, providing clear guidance on the procedures to be followed for faceless assessment, norms for accountability for calling information should be established;
- The assessments/appeals should be undertaken in a non-adversarial manner such that the rights of the taxpayers are not jeopardized;
- Further, SOPs for adjournment should provide for giving advance notice of say 15 days before next scheduled hearing;
- The functionality of the portal should be enhanced and upgraded. A window to upload large data without compromising readability and 24/7 access to the portal without technical glitches be provided. The taxpayer should be allowed to send his replies on one centralised mail id, in cases where the portal is not functional. This would enhance the user experience and will ensure timely submission of responses by the taxpayers;
- Adequate and reasonable timelines should be provided for furnishing the responses;
- Appropriate data security and confidentiality should be maintained since it is extremely critical to build greater comfort of taxpayers.

Other clarifications that may be considered by the CBDT to be issued in connection with the Scheme

- In case of matters remanded back by Tribunal or set-aside for fresh assessment, it should be clarified as to whether the assessment will be conducted by jurisdictional Assessing Officer or through the NeAC;

- It should also be clarified that the principle of judicial discipline will be followed by the ReAC. i.e. the ReAC would be bound by the jurisdictional High Court orders basis the jurisdiction of the assessee so that unintended litigation is avoided on this front.

1.6 Defer the proposal of Faceless Scheme for conducting Income Tax Appellate Tribunal (ITAT) proceedings for at least two years

Issues

- In line with the recent introduction of Faceless Assessment Scheme 2019, Faceless Appeal Scheme 2020, Faceless Penalty Scheme etc. Finance Act 2021 inserted new provisions under section 255 of the Act to enable the Central Government to frame a faceless scheme for conducting Income Tax Appellate Tribunal (ITAT) proceedings.
- Introduction of enabling provisions for faceless ITAT proceedings have given rise to lot of apprehensions in the minds of the taxpayers considering lack of experience in the field of faceless assessment and faceless appeal scheme introduced in 2020.
- The industry is yet to experience a full cycle of faceless assessment which has got delayed due to COVID 19 pandemic. The faceless assessment has run into legal challenges on lack of proper opportunity of hearing to the taxpayer.
- The ITAT is the last fact-finding authority in the appellate hierarchy for the income tax matters. When the facts are not properly appreciated by lower authorities, ITAT is the only forum for analysis of facts and legal issues and requires lot of advocacy in person. The Supreme Court and High Court admits and decides only on the question of law and not on question of facts.
- During COVID 19 pandemic, different benches of the Tribunals implemented protocols for virtual hearings. However, both Members and representatives of taxpayers and Tax Department faced many practical challenges in conducting the hearings.
- Government has already implemented almost all other tax proceedings in the faceless system. The taxpayers may face severe hardship if in-person hearings are not granted even at ITAT level.
- Given the fact that under the Faceless Assessment and Appeal Scheme, the opportunity of being heard is provided under exceptional circumstances with the approval of the higher tax authorities, it is anticipated that faceless ITAT proceedings may also provide for limited opportunity of being heard in person through video conferencing. This will adversely impact of cause of justice.

Recommendations

- It is recommended that considering the uncertainties of new system, the proposal should be deferred till the faceless system is fully stabilised for assessment and appeal proceedings. It should be deferred for at least two years to give taxpayers and Tax Department enough time to experience and equip themselves for faceless proceedings.
- Alternatively, if the scheme for faceless ITAT proceedings is to be implemented:-

- It is recommended that faceless ITAT be implemented for only low effect appeal matters in the initial phase, that too, at the option of the taxpayers, and other large cases be gradually covered in future.
- The scheme for faceless ITAT proceedings should also provide for adequate opportunity of being heard at all stages of the hearing. Video conferencing facility need to be liberally made available and not on discretion basis.

1.7 Withdraw deduction/collection of tax at a higher rate in case of non-filers of income tax returns

Issues

- Two new sections '206AB' and '206CCA' in the Income Tax Act introduced vide Finance Act 2021, mandates tax deduction or collection at a higher rate for non-filing of returns in the previous two financial years.
- Section 206AB is related to the higher rate of TDS and 206CCA is for TCS. This section will be in effect from 1st July, 2021.
- The higher rate is applied for certain notified taxpayers referred to as 'Specified Persons". "Specified Person" means any person who meets two conditions viz (a) who has not filed return for both of two assessment years relevant to the two financial years immediately prior to the financial year in which tax is required to be deducted and for which the time limit to file return under section 139(1) has expired and (b) the aggregate amount of TDS and TCS in his case exceeds Rs. 50,000 or more in each of these two preceding financial years.
- These provisions cast an additional responsibility on the payer to deduct higher rate of tax on payments to persons who have not filed their returns of income for one of the preceding two assessment years. This will create significant additional compliance burden on the taxpayer to check whether the deductee has filed its tax returns for the last two years. Though CBDT has introduced a new PAN based functionality to verify the compliance against above two sections. However, this functionality does not allow a real-time API based checking.
- Since the government already has the details of non-filers, existing machinery provisions of the Act can be used to achieve the objective of return filing. It is submitted that the compliance burden cast on industry should be commensurate with the benefits by way of higher revenue collection. The time and costs to be incurred by industry will be much higher than the TDS collected at higher rates and that too when Government already has data and statutory powers to pursue the non-filers. The new TDS/TCS provisions cast unreasonable burden on the industry and expose them to litigation, additional demands, interest, penalty, and prosecution risk. This adversely impacts the 'ease of doing business' in India.
- One may consider a listed company with lakhs of individual shareholders. It will be required to verify ROI filing compliance individually for each shareholder from e-filing website which will be extremely cumbersome and time consuming. The exercise will

need to be repeated at the time of each interim dividend and final dividend payment. This is because new shareholders may get added in the intervening period.

- The applicability of section 206AB of the Act on the non-residents having a Permanent Establishment in India is very theatrical and harsh for the industry. This has increased the compliance burden of all the payers significantly in terms of collecting necessary evidence from the non-resident vendors.
- In the absence of real-time API based functionality it becomes infeasible for E-commerce operators to check compliance towards an online real-time transaction. Recovery additional TDS/TCS from customer once the transaction is already executed would lead to financial loss to the E-commerce operator.

Recommendations

- Considering the unreasonable compliance burden on the industry, we strongly recommend that this provision should be withdrawn.
- Since the Government has the data with respect to PAN details of the taxpayer who do not file their tax returns, therefore it should reconsider whether such additional compliance obligations are needed.
- TDS on dividend under section 194 should be excluded for listed companies due to very high base of resident shareholders and strict timelines to pay dividend from record date.
- It is suggested that the department utility should be suitably uploaded so as to include only those non-residents in the specified person list who are actually specified person (i.e. capturing their Permanent Establishment status as well) and payer should not be under obligation to do any extra due diligence in this regard. Alternatively, non-residents may be exempted from the provisions of section 206AB of the Act.
- Nonetheless, till the time a real-time API based functionality is made available by CBDT to verify such compliance against a particular PAN the applicability of these provisions should be deferred.

1.8 Taxability of interest on employee's contribution to EPF in excess of Rs. 2.5 lakhs per annum

Issues

- Finance Act, 2021 has introduced a cap under section 10(11) and 10(12) of the Act where starting from 1 April 2021 interest earned with respect to employee contribution in excess of Rs. 2.5 lakhs per annum in a fund will not be eligible for exemption. Further the computation of interest ineligible for exemption has been prescribed by notifying Rule 9D of the Income Tax Rules, 1962 ('the Rules').
- Taxing such interest income on contribution to retirement fund without having enough social security system in place in contrast to other countries seems to be too harsh. India does not have a universal social security system applicable to all citizens and hence middle and upper-class taxpayers have to provide for their own social security.

- Provident fund has been traditionally a strong and safe avenue for salaried taxpayers to build up a retirement corpus to maintain the same standard of living and/or for life events like marriage of children or buying of new home, etc.
- As per Explanatory Memorandum to the Finance Bill, 2021, the amendment is intended to tax those employees who are contributing huge amounts to these funds and enjoying full exemption on interest on such funds. If the employee opts for PF, he is statutorily bond to contribute 12% of salary as employee's contributions. Hence, it is unfair to make distinction between contribution upto Rs. 2.50 lakhs and contributions in excess of Rs. 2.50 lakhs.

Recommendations

- The provision should be withdrawn. The interest income on the minimum mandatory contribution required to be deposited to PF by the employees should not be taxed even if it exceeds Rs 2.50 lacs. Alternatively, the limit of Rs. 2.5 lakhs for exempt interest income should be reconsidered and a higher amount should be provided.

1.9 Issues related to New Reassessment Regime introduced vide Finance Act 2021

Issues

- Section 147 to 152 of the Act, dealing with re-assessment of income tax proceedings, were revamped vide the Finance Act 2021 where inter alia, the new regime of reassessment permits reopening of assessments only on the basis of (i) information flagged in accordance with the Risk Management Strategy of CBDT; and (ii) final audit objections raised by the C&AG. In addition, the reassessment regime also provides a separate pre-assessment inquiry to be followed by Tax Authority before issuing notice for opening assessment of past years. Furthermore, even the time limitation periods have been reduced from the erstwhile 4/6/16 years (applicable in specified situations) from end of the relevant AY to 3/10 years from end of the relevant AY.
- In this regard, it may be noted that, under the erstwhile reassessment regime, the third proviso to section 147 of the Act reproduced below clearly restricted the powers of the Tax Authority to reassess matters which were subject matter of appeal, reference or revision:

  "Provided further that the Assessing Officer may assess or reassess such income, other than the income involving matters which are the subject-matter of any appeal, reference or revision, which is chargeable to tax and has escaped assessment."

- However, a comparative provision is conspicuous by its absence in the new reassessment regime. This may result in Tax Authorities trying to reopen assessments even in respect of matters which have attained finality causing needless litigation. Further, this may also vitiate the principle of tax certainty.

Recommendations

- In line with the professed stand of the government to reduce tax uncertainty, a clarificatory provision may be reintroduced prohibiting the tax authority from

undertaking reassessments w.r.t. issues which are subject matter of appeal, reference, or revision.

1.10 Expand the scope of Dispute Resolution Committee ("DRC")

Issues

- Finance Act, 2021 introduced a New dispute resolution scheme ("DRS") for resolving specified disputes in relation to specified Taxpayers and New Dispute resolution committee (DRC) to be set up to undertake dispute resolution in a faceless manner involving dynamic jurisdiction. Constitution of DRC and the overall scheme will be notified.
- The DRC will have powers to reduce or waive any penalty or grant immunity from prosecution where dispute is resolved through this forum.
- The scheme is available on a voluntary basis to Taxpayers and is alternate to appeals mechanism. Taxpayers will be provided an option for settlement of disputes arising due to a variation in the specified order in respect of a specified taxpayer who satisfies prescribed conditions:
    - The variation in the specified order should be less than or equal to 10 Lakhs (disputed amount)
    - If return has been filed by taxpayer for the AY relevant to the specified order, then the returned income should be less than 50 Lakhs.
    - The specified order should not have been passed pursuant to search or survey proceedings or pursuant of exchange of information under tax treaties/international agreements.
- The proposal was in deference to industry representations for mediation as an alternate dispute resolution forum and is welcome.
- However, the scheme is limited to small taxpayers where the returned income is less than Rs. 50 lakhs and disputed addition is less than Rs. 10 lakhs. The rationale for keeping out mid-sized and large sized taxpayers outside the proposed scheme is not clear.
- While it is stated that 'specified order' which can be resolved through DRC includes a draft order, it is not clear whether DRC can settle pending litigation cases satisfying the qualification criteria of returned income less than Rs. 50 lakhs and disputed addition less than Rs. 10 lakhs.

Recommendations

- It is recommended that the current threshold limits of returned income of Rs. 50 lakhs and disputed amount of Rs. 10 Lakhs should be eliminated to cover mid-sized and large sized taxpayers as well.
- It should also be clarified whether DRC can settle the pending litigation cases.

- The DRC must be constituted at the earliest with competent personnel and its performance must be monitored in terms of time-bound resolution of cases.

1.11 Issues regarding constitution of Board for Advance Ruling (BAR) to replace Authority of Advance Ruling (AAR)

- The CBDT has replaced the Authority for Advance Ruling with Board of Advance Ruling ('BAR') run by two members, each being an officer not below the rank of Chief Commissioner. Advance ruling pronounced by the BAR shall not be binding on either of the parties. Advance ruling pronounced by the BAR shall not be binding on either of the parties. A new provision on appeal is proposed to provide for an appeal from a ruling of the BAR to both the parties to the High Court, within 60 days of date of communication of the ruling. The 30 days period for withdrawal of application from date of application will continue to apply. Pending applications in respect of which no order has been passed before the notified date, such application along with all the relevant records, documents or material, on the file of the AAR shall be transferred to the BAR and shall be deemed to be the records before the BAR for all purposes.

Issues

- The relegation of the Authority of Advance Ruling to Board of Advance Ruling makes the system a lot less attractive to foreign taxpayers since the rulings are not binding and the process is no longer one which will be examined from the viewpoint of a fair and unbiased retired HC/SC judge. DRP is a good example, which consists of three CITs and yet it is very difficult for them to take an independent view considering the revenue impact of their decisions – they have inherent conflict of interest in discharging their functions. Foreign taxpayer may not apply to Board of Advance Ruling as there is an apprehension that decision may go against them.
- Non-binding nature of the advance ruling proposal will put the HCs overburdened as the applicant as also the tax department may file appeal in almost every case where the outcome of advance ruling is not in their favour.
- Since there is change in constitution of forum, the taxpayers whose applications are pending for a long time may no more wish to pursue their applications. The limitation of 30 days from date of application will preclude them from withdrawing their applications. It is not clear whether BAR will permit them to withdraw the applications as judiciously as erstwhile AAR – despite stiff opposition from Tax Department.

Recommendations

- A complete revamp in the scheme of advance rulings may not be warranted at this stage.
- Competent personnel may be appointed to man the AAR since the delay in delivering ruling was owing to the long vacancies in Chairman/Vice Chairman's office.
- An alternative resolution to the challenge faced in the existing scheme i.e. vacancy of the member at the Authority, would have been is to ease qualifications for appointing

the members from the Bar Council directly or include a President/ Vice-President of ITAT. This is similar to practice where several judicial members of the ITAT were elevated as judges in various HCs. Even industry/ tax experts from the non-government sector who can bring in specific expertise could be considered.

- This would help in speedy disposal of applications and at the same time, it would not hamper the independent functioning of the Authority. Both taxpayer and Tax Department will continue to have remedy of writ before HC.
- Without prejudice to the above, following are some specific recommendations in relation to functioning of BAR
  - The advance ruling should be made binding on the Tax Department.
  - It may be clarified that where neither of the party has gone into appeal against order of the BAR, the same becomes binding on both the parties.
  - The scheme for faceless functioning may not be implemented at this stage. This is because faceless determination of application without effective hearing may lead to erroneous determination. The same may be implemented based on the experience gained on faceless assessment and faceless CIT(A).
  - The admitted applications should be heard in entirety by current AAR itself.
    - With prejudice, in case pending applications are transferred to the BAR and the applicant wishes not to pursue application with the BAR, the application may be allowed to be withdrawn at any stage of the proceedings. The application fee may be refunded to them after deducting certain portion.
    - If two members of BAR have disagreement, there should be an enabling provision to solve such disagreement.
    - There is also a need to ensure that consistency in rulings is maintained between the different benches of BAR. Different benches must be consistent in the approach and must follow the Orders passed by the coordinate benches.
    - Since the taxpayers applied to AAR for expeditious resolution of contentious issues, the time limit for completing assessment after withdrawal of application or pronouncement of BAR should be reduced to six months from such withdrawal or pronouncement.

1.12 Extend time to file revised/belated return

Issue

- Finance Act 2021, in an effort to provide tax certainty reduced various time limits for compliances and assessment procedures. Amongst others, the time limit for filing a revised return under section 139(5) and belated return under section 139(4) were curtailed to 31 December of the same Assessment Year.
- The timeline for filing of original return in case of assesse liable to audit under section 92E of the Act is 30th November of the assessment year and the revised timeline for

filling of revised or belated return will be 31st December of the assessment year. Thus there would be only one month difference in filing of original return and belated/ revised return from a period of four months earlier. This reduction in time gap defeats the purpose of permitting the taxpayer to file a revised return. In other words, this timeline is insufficient and doesn't give assessee sufficient time to rectify the error and omission, if any occurred while filing original tax return.

- Further, in many cases, taxpayers having foreign income which is taxed abroad may not have clarity on the amount of tax paid/payable overseas within the time permitted for filing revised/belated return, leave alone at the time of filing original returns. This is because India provides FTC only in respect of taxes paid in the year in which the corresponding income is offered for tax.
- This above would be especially true in respect of countries following a calendar year for tax purposes where the income for the period from January to March would be assessed to tax in the foreign country after the period for filing of revised/belated return in India has already expired. This may cause serious hardship to taxpayers claiming FTC as it would result in double taxation and/ or cash flow issues.

Recommendations

- It is suggested to restore back the original time limit for filling of revised/belated tax return to 31st March of said assessment year.
- Given the above, it is recommended that the period for filing revised/belated return be extended at least in respect of taxpayers claiming FTC to enable them to make the claim once the tax is paid in the overseas jurisdiction. This would also be in line with India's obligations of providing a fair and equitable taxation system as also treaty obligation to avoid double taxation of the same income.

1.13 Rationalise TDS provisions for payments to non-residents to allow for treaty benefits

Issue

- The SC in case of PILCOM v CIT [2020] 425 ITR 312 held that where a withholding provision under Chapter XVII-B of the Act provides for specific rate for withholding of taxes, the taxes shall be deducted at specified rate only and provisions of DTAA shall not be taken into account.
- The ratio of this SC ruling required payer of income in respect of securities to FII to deduct taxes at the rate prescribed in S. 115AD i.e. 20% even where FII was eligible to claim DTAA benefit and DTAA provided for lower rate of taxes.
- Post SC ruling in case of PILCOM (supra), several representations were made to CBDT to allow the payers to deduct the taxes at the rates provided in DTAA while making payment to FII and also other non-resident payees wherever the relevant TDS section provides for fixed rate of TDS and not at 'rates in force'. List of such other sections (such as S. 194LC, 194LD, etc.) impacted are provided in Table below.

List of Sections providing for specified rate of deduction to Non-Residents

S. No.	Section	Particulars	Withholding rate (excluding surcharge and cess)
1.	194E	Payment to non-resident sportsmen/ sports association	20%
2.	194LB	Payment of interest on infrastructure debt fund	5%
3.	194LBA (2)	Payment of interest and dividend income by business trust	5%/10%
4.	194LC	Payment of interest by an Indian company or a business trust in respect of money borrowed in foreign currency	5%/4% (IFSC unit)
5.	194LD	Payment of interest on rupee denominated bond of an Indian company or government securities to a foreign portfolio investor	5%
6.	196B	Income from units (including long-term capital gain on transfer of such units) to an offshore fund	10%
7.	196C	Income from foreign currency bonds or Global Depository Receipts (GDR) of an Indian company (including long-term capital gain on transfer of such bonds or GDR)	10%

- In deference to representations made, FA 2021 inserted a proviso to section 196D(1) of the Act to provide that, payer shall withhold tax at the rate of 20% or rate specified in DTAA (whichever is lower) where,
  - DTAA entered between India and other country is applicable to FII payee
  - Payee has furnished tax residency certificate
- While the amendment is welcome and addresses the difficulty for FIIs, it is not clear why other non-residents are not granted similar treatment. The application of TDS at higher rate compels the payees to file returns to claim refund of excess TDS. In many cases, the payments are made on 'net of tax' basis and TDS at higher rate results in higher cost for the residents since the NR payees are not inclined to file returns to claim refund of excess TDS.
- As a matter of tax policy, India has, till date avoided the policy of 'retain and refund', and has consistently adopted a tax policy where TDS is restricted to the amount of the actual tax liability incurred by the non-resident recipient of income. This has eased compliance

on the taxpayers as also administrative burden for the Tax Department. The amendment to section 196D of the Act is consistent with this policy.

- Such tax policy, if continued to be applied for other sections as well, may harmonize with the thinking that TDS is secondary tax obligation and should ideally follow the primary tax obligation. In order to avoid any form of differentiation or discrimination, the tax policy may adopt procedure which, on principles, treats all the taxpayers at par.

Recommendation

- Amendments on lines of proviso to section 196D(1) of the Act, may be made to all other provisions which provide for fixed rate of TDS for payments to non-residents in order to allow the non-resident taxpayers take benefit of the lower tax rates provided in the respective tax treaty.

1.14 Applicability of Section 44ADA to Limited Liability Partnership (LLPs)

Issues

- Section 44ADA of the Act is special provision for computing profits and gains of profession on presumptive basis. As per section 44ADA, where a resident assessee is engaged in a specified profession and whose total gross receipts do not exceed fifty lakh rupees in a previous year, a sum equal to fifty per cent of the total gross receipts of the assessee in the previous year on account of such profession or, as the case may be, a sum higher than the aforesaid sum claimed to have been earned by the assessee, shall be deemed to be the profits and gains of such profession chargeable to tax under the head "Profits and gains of business or profession".
- Presently, the section 44ADA is available for all resident taxpayers engaged in specified profession.
- The Finance Act, 2021 has denied benefit of presumptive taxation under section 44ADA to LLPs.
- For the purpose of the Act, partnership firms and LLPs are treated in same manner. The term 'firm' includes partnership firms as well as LLPs. Benefit of presumptive taxation should not be denied to LLPs, when such benefit is available with partnership firm.
- Threshold of Rs. 50 lakhs provided under section 44ADA is sufficient to protect interest of revenue. Even though LLPs are required to maintain books of accounts under the LLP Act, the determination of taxable income, claim of deductions for expenses and allowances, production of evidences, etc. are burdensome procedures which may create unnecessary compliance burden for LLPs. There does not appear to be any justification whatsoever to discriminate against the LLPs as opposed to partnership firms as the LLP law is a much progressive law and encouragement needs to be provided to them. This will also facilitate ease of doing business and less compliance burden. Hence LLP taxpayer should be allowed to claim benefit of presumptive taxation under section 44ADA of the Act.

Recommendations

- LLPs should be allowed to offer professional income on presumptive basis under Section 44ADA of the Act.

1.15 Provide clarification regarding applicability of definition of 'Liable to tax'

Issues

- Section 90/90A of the Act allows the taxpayer to claim benefit of tax treaty entered by Indian Government with other countries to avoid double taxation. The benefit of treaty would be available only to the persons, who are resident of the either of the treaty country. Generally, treaties define the term 'Resident' as a person who is 'liable to tax' in a country by reason of domicile, residence or any other criterion of similar nature. Presently, neither the Act nor the treaties define the term 'Liable to tax'. The Finance Act, 2021 has defined the term 'Liable to tax', which shall cover following two scenarios:

  - There should be an actual liability of tax on such person under law for the time being in force;
  - It shall include a case where subsequent to imposition of tax liability, an exemption has been provided.

  The definition would apply not only for the purpose of the Act, but also for the purpose of tax treaties.

- Consider case of pass-through entities, wherein the partner or members are liable to pay taxes on their respective share of income. Such pass-through entities cannot be held as 'liable to tax'. As a result of which, such pass-through entities would not qualify as 'Resident' of either of the contracting states of the tax treaty and accordingly, they might be deprived from treaty benefits.

Recommendations

- It is recommended to restrict applicability of the term 'Liable to tax' for the purpose of the Act only.
- Without prejudice to above, clarification can be issued to avoid unintended denial of tax treaty benefits to pass-through entities.

Annexure to Section I

Issues related to Equalisation Levy

Restrict scope of EL to cases where all or substantially all/majority of activities have taken place online

Background and issue

- In today's world, every business (including traditional brick and mortar business) has embraced technology to bring greater efficiency to its business operations. The technology could be adopted with various different goals in mind. Very often, technology is being used to make the activity more time and cost efficient (e.g. collection of Purchase Orders through an online link as against emailing or posting), or as a mode of communication (e.g. email for correspondence as against letter or phone call), or collection payment (e.g. weblink to make payment as against a wire transfer), or receipt of inquiry on company's website which would be construed as acceptance or placing of order (e.g. inquiry box or contact us links).
- Where traditional or digital business participate substantially in India's vast market through digital means, India could certainly look at a recompense for erosion of its tax base where laws are not sufficient to create a taxable nexus. It is, therefore, important to determine what will constitute such digital nexus that ought to be taxed.
- Finance Act, 2021 expands the scope of 'online sale of goods' or 'online provision of services' to one or more of the following online activities viz. (a) acceptance of offer for sale; or (b) placing of purchase order; or (c) acceptance of the purchase order; or (d) payment of consideration; or (e) supply of goods or provision of services, partly or wholly.
- The amendment widens the scope of EL provisions to physical/ offline supply of goods and services where any one of the specified activities take place online. Such approach perhaps has an unintended, and certainly undesirable, effect of covering traditional businesses wherein technology plays only an incidental or trivial role. In such cases, the digital or electronic facility is utilised not for availing the principal goods or service but merely for seeking information or for confirming the booking or simply streamlining supply chain. The primary object of such business continues to be purchase of physical goods or availing physical services.
- Such a wide scope does not align with global discussion with regard to digital economy taxation. Most of the Digital Service Taxes (DST) imposed or proposed by various countries are restricted to digital goods or services.
- It may also be noted that the unusually wide ambit of India's EL is criticised in investigation report issued by the United States Trade Representative (USTR) under Section 301 of the Trade Act, 1974. India's response to this particular observation has been that India is seeking to tax only those transactions which have sufficient

nexus with India that would have otherwise given it taxing rights. This argument may get diluted with the broad expanse now the levy would have post amendments.

- It virtually taxes all activities which constitute 'business with India' rather than taxing activities constituting 'business in India'. There will hardly be any import of goods or services which will not involve any of the above referred specified online activities. In the least, all payments for imports of goods or services are made through digital channels involving some payment facility through digital or telecommunication network.

Recommendations

- In terms of Explanation to section 164(cb), the applicability of EL should be restricted only to those cases wherein all or substantially all activities take place online.
- It should also be clarified that the intent is to tax e-commerce transactions and therefore, instances such as online ordering systems (or such similar internet based systems), or Enterprise Resource Planning (ERP) software, or corporate websites through which orders are received, or purchase orders received vide emails or a common portal (such as a document management and storage system) using the internet, through which orders are received by non-residents, should not be brought within the ambit of EL, only because they use telecommunication network for such interaction. Such systems are used only as a means to achieve operational efficiency and not to effectuate sales or solicit customers. In other words, the ambit of provisions should exclude what is not normally regarded as "e-commerce", e.g. email, ERP, intranet, etc.
- Provide also clarity that functions which were traditionally being carried out offline and have been made online only due to Covid-19 travel restrictions should not be covered within the ambit of EL.

Consider providing a specific exclusion for payment gateways/payment aggregators

Background and issue

- Given the expanded scope of EL, the non-resident banks or payment gateways, or aggregators may be liable to EL, even though they are only facilitating payment leg of the transaction for an offline transaction or a transaction facilitated by another e-commerce operator.
- Promoting digital payments is one of the policy initiatives placed by the Government. To give impetus to digital payments, the Honourable Finance Minister in her Budget Speech 2021 declared that an amount of INR 1,500 Crores will be earmarked to promote digital mode of payments. Thus, the Government itself has been incentivizing the taxpayers to use digital mode of transactions. In such situation, it may be contrary to the Government's initiatives to levy EL on transactions merely on the ground that payment has been made online or through digital means.

- Further, it may be difficult, rather impossible, for the payment processor to determine whether the consideration is chargeable under EL, for instance, whether it is in the nature of royalty/ fees for technical services (FTS), if subjected to advertisement EL, etc. It is also difficult for the payment processor to determine whether other NR e-commerce operator is liable to EL and is making payment of EL on the same transaction.

Recommendations

- Without prejudice to our representation to restrict the levy only to digital goods or services, it is requested to eliminate clause (d) of Explanation to section 164(cb), viz. “payment of consideration”. Alternatively, a specific exclusion for payment gateways/ payment aggregators should be considered. It should at least be clarified that transaction is not covered under ESS EL if entire transactions takes place offline (booking, acceptance, confirmation, delivery) but payment take place online.
- Also clarify that where the payment gateway is collecting monies from an Indian resident on behalf of the non-resident ecommerce operator, it is in-effect providing collection services to the non-resident ecommerce operator under their agreement. Indian resident, if at all, is merely agreeing to the terms of use of payment gateway operator. Therefore, such transaction should not be subjected to equalisation levy.
- Reference may be made to clarification provided at para 4.2 of Circular No. 17/2020 dated 29 September 2020 in the context of TDS under section 194O where it is clarified that payment gateway will not be liable to do TDS if tax has been deducted by the e-commerce operator on the same transaction. Similar logic will apply even in context of EL except for the aspect that it may be difficult for payment processor/gateway to find out whether the recipient is NR E-commerce operator and whether such NR E-commerce operator is liable to EL. In any case, the payment processor/aggregator merely provides payment service and the scope of EL should not extend beyond consideration receivable for such payment services.

Clarify that EL will not apply where services are availed outside India

Background and Issue

- Consider a scenario where the services of overseas hotels are booked online, and the actual accommodation services consummated outside India. In such cases, the contract is for use of room rights and not rendering online services of booking. The broad scope of EL covers such situations merely on the premise that booking takes place online from India or is done by a person resident in India.
- Place of consumer is the very basis of granting taxing rights to market jurisdiction as per the ongoing debate in the context of digital economy. Coverage of such situation within the realm of EL may amount to extra-territorial application of the law.
- Even under the existing source-based taxation principles, the FTS/ royalty payments which are for the purpose of business or source outside India are not subjected to tax in India. The broad scope of EL may also cover unintended cases where FTS/

royalty payments meant for business outside India is not taxable in India by virtue of source rule exclusion under ITA but is subjected EL because order is placed online or payment is made online from India.

- Also consider a scenario where an Indian resident reserves a ticket for a theme park attraction or a natural wonder or sports event or a theatrical performance outside India and pays for it online. The services of the physical attraction are availed physically outside India. Now the entire reservation fees could be subjected to EL India only because payment was made online.

Recommendations

- The scope of EL should exclude cases where objects of consumption are outside India and the physical consumption of goods or services, therefore, takes place outside India.

Clarify that internal goods/services management systems are not covered by the levy

Background and issue

- Both traditional and new economy organisations employ various electronic systems in the form of ERP, content management systems, inventory management including Just-in-time systems, workflow systems, accounting, payroll and compliance management, knowledge sharing and information systems, etc.
- All these systems are primarily driven towards promoting efficient business operations. For example, the system may make it more efficient to place an order which could otherwise be placed through physical means or over a telephone or email. R&D in pharma industry or solutions in consulting industry could be more easily be accessible over internal systems by the group companies. These systems are used for faster & reliable communication, elimination of human error and saving of operational costs.
- The scope of EL perhaps unintentionally may extend to these systems.

Recommendations

- A clarification may be provided that such systems do not constitute e-commerce and therefore, will be excluded from the purview of EL.

Clarity on terms "acceptance", "offer for sale"

Background and issue

- Amendment employs the terms such as "offer for sale", "acceptance" or "placing" of purchase order. Presently, there is no clarity as to the scope and coverage of these terms. It is possible that in some businesses entire negotiation of agreement takes place offline and the necessary documents are sent online or uploaded on an internal system. In such circumstances, there is an apprehension that mere sharing

of relevant documents may tantamount to placement of purchase order or acceptance of offer for sale.

Recommendations

- Suitable clarifications should be provided in this regard. It may be clarified that mere “receipt” of purchase order or offer for sale is excluded from the scope of the levy.

Clarify that EL is restricted only to the convenience fees earned by the e-commerce intermediary for facilitating the transaction

Background and issue

- E-commerce operators are liable to 2% EL on the amount of consideration “received or receivable” from e-commerce supply or services. The amendment under section 165A(3)(b) appears to impose EL on the gross consideration collected by intermediary/ aggregator.
- It may be noted that when the aggregator/facilitator collects consideration from the customer, it collects the same on behalf of the seller/service provider (e-commerce participant) and has no right over such consideration. The intermediary is entitled only to commission or facilitation fees as a consideration for its facilitation or marketplace services. In such situation, to impose a levy on a consideration which does not even belong to the e-commerce operator may not be fair and justified.
- Also consider an instance where Indian resident makes an offer for purchase of an overseas property online, and thereafter consummates the deal offline. EL may bring to tax the entire value of the property to tax in India.
- This may also impact eligibility of aggregators to claim *de-minimis* exemption of INR 2 crores under section 165A(2)(iii) if the consideration received on behalf of e-commerce participants is reckoned to the account of e-commerce operator. Also, where non-resident seller or service provider has a PE in India, EL on gross consideration may result in application of EL despite the exemption under section 165A(2)(i).
- Further, taxing gross consideration may result in duplicated levy wherein the e-commerce participant itself is liable to EL for the consideration received for online sale of goods or online provision of services. Also, in certain cases, online sale transaction may take place through multiple e-commerce operators and charging EL to each such operator may result in multiple taxation with cascading effect leading to increased cost of the transaction.

Recommendations

- The amendment in section 165A(3)(b) on the scope of consideration received or receivable” should be omitted.

- It should be clarified that the amount of consideration received or receivable by the e-commerce operator for facilitating the transaction will be restricted to convenience fees received or receivable by such operator in its own rights.
- Without prejudice to the above, aggregator/ facilitator should be relieved from compliance with EL to the extent of value of third party supply it has facilitated, where the payment has not been routed through the operator. Equally, third party supplier cannot be asked to make good on EL liability of the aggregator/ facilitator.

Specific relief to seller or service provider if the aggregator or intermediary discharges EL on the gross consideration

Background and issue

- As indicated above, the seller or service provider itself may be liable to EL if qualifies as e-commerce operator. Thus, there is a possibility of duplicated collection of EL.

Recommendations

- In such cases, if levy is imposed with reference to the gross consideration, a specific relief should be provided to the seller or service provider from its own EL obligation. For this purpose, the seller or service provider may obtain a declaration similar to the one sought by payment gateways in the context of section 194O (refer Circular No. 17 of 2020 dated 29 September 2020).
- Further, it should be clarified that such seller or service provider will be eligible for exemption under section 10(50) of the Act once the transaction of online sale of goods or provision of services has been subjected to EL on gross basis. If seller or service provider is otherwise taxable under the Act, denial of exemption may result into double taxation, which is contrary to the intent of providing exemption as supported by Explanatory Memorandum to FB 2016.
- Also, if levy is imposed on the gross consideration and the obligation to discharge EL is on the aggregator or intermediary, payment challans and Form 1 be appropriately amended to capture the details of the seller or service provider on whose consideration EL is paid by the aggregator or intermediary.

Specific relief from withholding under section 194O where EL is charged by aggregator or intermediary on the gross consideration

Background and issue

- In terms of section 194O, the e-commerce operator is obliged to withhold taxes on the gross amount of sale or services by the e-commerce participant. Thus, where e-commerce operator is required to discharge EL on gross consideration, there will be duplicated obligation on the e-commerce operator to pay EL as well withhold tax under section 194O of the Act.

Recommendations

- The intent of section 194O as expounded in the Explanatory Memorandum to FB 2020 is to widen and deepen the tax net by bringing participants of e-commerce

within tax net. Thus, once EL is discharged even on the part of consideration earned by e-commerce participant, it is fair to exclude such transactions from the gamut of withholding obligation under section 194O of the Act.

"Consideration received or receivable" to exclude sales returns, collections of taxes on behalf of Government, such as GST, service tax or alike

Background and issue

- In case of sales of goods or services by e commerce operator, sales returns are very common in both retail and wholesale scenarios. In certain categories like fashion merchandise, the returns can be as high as 25% of the sales. Refunds are also common either due to certain technical issues or non-delivery of standard services to the customers.
- Further, in the context of various TDS provisions, CBDT has clarified that consideration for a given service is to be calculated without taking into account statutory levies which are collected for handing over to the Government. Refer CBDT Circular No. 1/2014 for service tax on rent and professional services, CBDT Circular No. 23/2017 on GST and para 4.3.2 of Circular No. 13/2021.

Recommendations

- Accordingly, without prejudice to our representation in the above paras, it would be fair to restrict levy to consideration towards net consideration received or receivable. Also, the e-commerce operator should be permitted to make adjustment of sales returns and credit notes in the quarter of the financial year to which it pertains while doing quarterly compliance under section 166A of the FA 2016. The fact that the related sale may pertain to earlier quarter may not be relevant consideration while granting reduction so long as such sale was considered for ESS EL in the earlier quarter. Please note that TCS under CGST Act 2017 is also calculated with reference to net value of taxable supplies" after reducing the aggregate value of taxable supplies returned to the suppliers during the month.
- Further, a suitable clarification may be provided that ESS EL will be levied with reference to consideration flowing to the operator and will exclude collections on behalf of Government such as GST.

Instructions for Indian resident payer

- It is quite possible that there will be several transactions where there could be debate on applicability of EL vis-à-vis royalty/FTS.
- It is also possible that Indian resident payer may decide to err on the conservative side and withhold income tax on the payment by treating as royalty or FTS only to protect against adverse consequences of failure to withhold taxes.

Recommendations

- It should be clarified that where non-resident has duly discharged EL on its receipt and evidenced it to Indian resident, then Indian resident payer should not be

considered as an ‘assessee-in-default’ and should not be made liable to consequences of failure to withhold taxes. Form 15 CA/15 CB procedures could carry suitable disclosures to this extent.

- Indian tax authorities will in any case have the opportunity to audit the EL compliances made by the non-resident and where for any reason royalty/ FTS characterisation or existence of PE is determined, EL paid should be adjusted against tax demand raised to prevent undue hardship.

Clarifications are ‘retrospective in nature’ and without prejudice, they should come into effect only from FY 2021-22, except applicability of section 10(50) of the ITA

Background and issue

- The EL were introduced at enactment stage as a surprise package and without any supporting Memorandum or clarificatory document. Given such situation, the taxpayers have been grappling with the interpretational issues and procedural hurdles. Stakeholders had been seeking clarifications time and again to gain clarity and certainly with regard to the applicability of the levy.
- The Government, vide Finance Act, 2021, has enacted certain amendments with retrospective effect from 1 April 2020. The Explanatory Memorandum to FB 2021 states that the amendments to EL have been introduced with a view to provide *“clarifications to correctly reflect the intention of various provisions concerning this levy”*.
- It may be noted that the amendments are substantive in nature and significantly widen the scope of EL provisions. The amendments have resulted in covering the business models which were otherwise outside the net of EL; also the base of levy has underdone change by virtue of the amendment to “consideration received or receivable”. Such amendments are causing significant hardships to the taxpayers with no breather to comprehend the provisions and immediately comply with the same.

Recommendation

- The present Government has always fostered the policy of prospective amendments. Aligning with such philosophy, the amendments to EL chapter (except applicability of s.10(50)) should be made prospective with effect from 1 April 2021 (FY 2021-22). Retrospective amendments negatively impact the sentiments of the stakeholders.

Provide for protection from interest and penalty under ITA as well as EL

Background and issue

- On account of retrospective amendment, following issues may arise:
    1. Additional EL liability for the e-commerce operator who adopted a view that EL is restricted to digital goods and services alone

ii. Additional EL liability for intermediaries or aggregators who discharged EL on the net consideration received

iii. Income-tax liability to e-commerce operators who claimed exemption under s.10(50) with respect to royalty/ FTS income

iv. Withholding tax liability to payers of royalty/ FTS who did not deduct tax at source relying on s.10(50) exemption

Recommendation

- For above referred genuine cases, it should be explicitly clarified that no interest and penalty will be levied for additional income-tax or EL or withholding tax liability arising pursuant to the retrospective amendments.

Other points for consideration

Clarify explicitly that EL is an interim measure and will be abolished once global consensus under BEPS 2.0 is in place

Background and issue

- The blueprints of unified approach under BEPS 2.O have already been released and there is a strive and commitment to achieve global consensus by end of 2021. The public discussions and stakeholder consultations in this regard are in progress.
- The efficacy of such global measure is highly dependent on uniform approach to be adopted by each member country. Any unilateral measure is not only inconsistent with global agenda but is also likely to result in undesirable multiple taxation of same income without any tax credit or an effective opportunity of eliminating such multi taxation. India has, time and again, even while vocalising its view point vociferously, expressed solidarity and support for the OECD led solution for taxation of digital ecommerce.

Recommendations

- In tandem with the above global spirit, it should be clarified that EL is a transit/ temporary/ interim measure. An explicit statement to this effect will send assuring signals to the investors particularly as the scope of EL as now applicable is fairly wide.

Terms “goods” and “services” should be defined to exclude financial instruments, insurance, forex derivatives, actionable claims, shares, securities, bonds, debentures, etc.

Background and issue

- ESS EL applies to online sale of goods or online provision of services or facilitation thereof. The terms “goods” or “services” are not defined.
- Reference can be made to definitions under CGST which exclude share, securities, money, actionable claims from scope of TCS.

Recommendations

- Thus, it is recommended to introduce suitable definition to exclude certain terms like shares, securities, money, actionable claims from scope of “goods” and “services”

Clarity on “sale of advertisement”, “sale of data” between two non-residents:

Background and issue

- **Sale of advertisement between non-residents -** The expansive language of the provisions could potentially cover a wide gamut of transactions between non-residents. The language of clause (i) of Section 165A(3) also covers situations where an online advertisement is merely accessed by persons in India, who were not the target audience for such advertisement at first place.

  Further, through advertisements, enterprises may intend to target markets region-wise rather than a specific country (say, India). This creates a complexity as to how much consideration for the sale of advertisement shall be allocated to persons accessing the advertisements in India and outside India.

Recommendations

Clarity should be provided on the scope and exclusions from the provision and rule out the possibility of it extending to unintended situations. We also request that clarity be provided with respect to the India allocation of sale consideration where the advertisements are more widely targeted. It should be clarified that the levy will not trigger if while browsing New York Times, a person is resident in India finds a general/static advertisement of US products (not specifically meant or designed for Indian). Also, depending on pricing model, it may so happen that ad revenue is not earned only when a customer clicks on the ad. In such cases, the revenue cannot be attributed to the Indian customers who merely views the advertisements but does not click on it.

Reference can be made to the draft guidance released under France Digital Service Tax (DST) which provides guidance on what is “targeted advertising”. According to the said guidance, “targeted advertising” is characterized by three cumulative conditions:

(i) services are marketed to advertisers or their agents;

(i) advertising messages are placed on a digital interface; and

(ii) the messages are targeted based on users data (either collected on the interface itself or collected/generated when users consult other digital interfaces).

The guidance clarifies that targeted advertising messages are designed, at least partially, based on data from the user of the digital interface on which the message is placed. Such data, notably keywords in a search engine, identification username or password and personal or non-personal data, could have been collected on any digital interface. However, it does not apply in cases where the data is not collected or generated via digital interfaces; data that have no influence on the recipient or

the content of the advertising message; and data related to the digital interface itself but not specifically related to the user of the digital interface.

Background and issue

- **Sale of data between non-residents -** Clause (ii) of Section 165A(3) aims to apply the EL on transactions relating to *"sale of data collected from a person who is resident in India or from a person who uses internet protocol address located in India".* While the language is clear to include only sale or disposal of data transactions, the language does not specify the nature of 'data' sought to be covered by the provision. Further, the provisions purport to tax sale of data irrespective of whether it was collected in the past.

Recommendations

The nature of 'data' intended to be covered should be clarified. Clarification should also be provided to with respect to the period to which the 'data' relates.

Further, some users may not provide the correct contact information, thereby, making it all the more difficult to ascertain if the data is collected from persons resident in India. It is requested that suitable clarification be brought in to address this issue as collation of reliable information and attribution thereof is almost impractical.

Guidance on determination of IP address, residential status[3]

Background and issue

- As per section 165A(1)(i), ESS EL shall be charged on the amount of consideration received or receivable by an e-commerce operator from e-commerce supply or services made or provided or facilitated by it to a 'person resident in India' or a person using IP address in India.
- Whether a person is a resident or not in India is a fact specific exercise and may be challenging for the 'e-commerce operator' to verify the residential status for its customers. Further, it may be impractical for companies to keep track of the IP address of every user and data flows. It also raises questions regarding whether the IP address requirement is sufficient, reliable and verifiable indicator of nexus in all cases. There could also be security concerns while adopting IP address as criteria to trigger ESS EL (e.g. a hacker to sabotage the company by a DDoS attack (or a method of masking IP address) can create a risk for company)

Recommendations

- Thus, it is imperative that a guidance about determination of IP address and determination of a residential status of a person is provided.

[3] For instance, in case of a non-resident University/ Education institute, student travel to and fro from India

Appeal remedy against all EL disputes

Background and issue

- Presently, remedy for filing appeal only against order imposing penalty under EL for default in deduction or payment of EL and/or filing of annual statement.

Recommendations

- Therefore, appeal remedy should also be available for any EL disputes.

Scope of 163 to be made restrictive for the purpose of EL

Background and issue

- Section 178 of the FA 2016 states that the provisions of Chapter XV of the ITA shall so far as may be, apply in relation to equalisation levy, as they apply in relation to income-tax. Chapter XV of the ITA provides liability in special cases and includes provisions with regard to representative assessee as well. Section 163 of the Act which provides meaning of agent with respect to non-resident provides various limbs and one such limb covers a person in India from or through whom the non-resident is in receipt of any income, whether directly or indirectly (S.163(1)(c) of the ITA).

Recommendations

- It may be noted here that the reason for shifting the compliance burden on NR for ESS EL is due to the fact that it captures even B2C transactions and making every customer who is in receipt of online sale or supply of services as agent of NR can become clumsy and non-feasible. On similar basis, it is prayed that limb (c) can be deleted or modified in a manner that liability of representative assessee is not cast on the customers in case of B2C transactions.

Set off of EL liability against liability under the Act and vice-versa. Also, provide clarity on refund mechanism for excess EL liability paid

Background and issue

- There can also be a situation where the non-resident e-commerce operator pays EL on the basis that there exists no PE in India, however in appellate proceedings, it is finally concluded that e-commerce operator has a PE in India and hence the income is taxable under the provisions of ITA and not under FA 2016 due to s.165A(2)(i). Similarly, situation may arise where tax department alleges that the payment is royalty/FTS and in appellate proceedings the payment is held as not subject to EL but liable to tax as royalty/FTS under the provisions of ITA.

- It is also possible that Indian payer may approach the Indian Revenue under s.195 for determination of appropriate taxes where non-resident ecommerce operator has already discharged ESS EL and represented such income to be eligible for exemption under s 10(50).

- In such cases, an issue arises as to how should the EL tax which has been paid initially by the e-commerce operator be treated. Currently, there appears to be no mechanism for e-commerce operator to claim credit or refund for ESS EL already discharged.
- As per the return format prescribed for the non-resident e-commerce operators

  (Form No 1), excess payment of EL is required to be claimed as a refund. However, there is no clarification/guideline issued regarding the process of claiming refund. Further, there is no option given for furnishing the bank account details while filing the return with refund claim. It may be noted that the time gap provided for making the EL payment is just 7 days for the first three quarters, and in the case of last quarter, non-resident e-commerce operators are required to deposit EL by the last day of the quarter itself. Because of such a tight timeline, most of the time, payments are based on the estimate, resulting in excess/short payment of EL.

Recommendations

- It is recommended that in the absence of any clear directions in this regard, the amount paid as EL should be treated as advance tax for ITA purposes and accordingly, the amount should be available for set off/ adjustment against the income tax payable under the ITA.
- Further, as a corollary, it should also be clarified that in a case where resident payer, conservatively withholds @ 10% as royalty/ FTS while the payee believes it is liable to EL, a credit of 10% withholding tax against EL liability of 2% (as also facility to claim of refund of excess 8% taxes) should be available through EL annual return itself. This will eliminate the concerns over cash blockage for taxpayer to the extent of tax withheld by the payer (since otherwise NR e-commerce operator will have to claim refund of taxes withheld in the ROI).
- It is requested that necessary amendment be made to enable the self-adjustment option in the case of excess payment of EL. Under the self-adjustment option, non-resident e-commerce operators should be allowed to adjust the extra amount with subsequent period liability.

Background and issue

- As per Section 166A, every e-commerce operator is required to pay EL to the credit of the Central Government for the quarter of the financial year within the due dates specified. While in respect of quarters ending in June, September and December, the due dates for deposit of EL are 7 July, 7 October and 7 January, respectively in respect of the quarter ending 31 March, the due date to deposit EL is 31 March itself.
- As per the general business practices, the sales reports are generated/ finalised in 3-4 working days after the end of the month. Basis such sales reports, the amount of ESS EL shall be calculated and finalised. Further, the NR needs to remit the payment to Indian banks for subsequent payment to the Indian treasury which further consumes time.

Recommendations

- Given that the e-commerce operator will be required to assess transactions and amounts on which EL is required to be discharged which may take time, it is prayed that the due dates for making the payment of ESS EL should be relaxed to 30 days after the end of each quarter.
- Without prejudice, it is recommended that at least the due date for the March quarter is specified as 30 April, same as the due date for deposit of TDS for March quarter.

Section II

Suggestions to boost Growth, generate Employment and COVID-19 Related Relief Measures

2.1 Reinstate 200% weighted deduction for in-house R&D expenditure under section 35(2AB)

Issue

- With the changed business scenarios and disruption in business across all industries due to COVID -19, there is need to step up the Research and development activities. The present situation shows the importance of R&D to come out with new or cheaper versions of medicines for Indian and export markets. Also, the research and development have to be incentivised going forward if the Government wants to achieve the objective of Atmanirbhar Bharat and Make in India. Several countries have low corporate tax rates along with R&D incentives, e.g. Singapore (Tax rate 17 percent further reduced to between 5 to 10 per cent in respect of qualifying IP income; 100 to 250 percent of R&D expenditure), China (Tax rate 25 percent reduced to 15% in respect of High and New Technology Enterprise; 170 percent of R&D expenditure); UK (Tax Rate 19 percent; Patent box regime to encourage R&D).
- The hitherto available tax benefit by way of weighted deduction @ 150% (substituted for 200% vide Finance Act 2016 w.e.f. 1 April 2018) for DSIR approved in-house R&D centres has expired on 31 March 2020.

Recommendation

- There is a need to extend the benefit to provide fiscal stimulus to innovation in industry. It is therefore recommended that weighted deduction @ 200% under section 35(2AB) of the Act be restored to promote research and development in the manufacturing space and to make India a manufacturing hub.
- The deduction should be made available even if company avails lower tax rates under section 115BAA or 115BAB of the Act. Alternatively, provision of research tax credit may be introduced.

2.2 Enhance section 80JJAA qualifying employee remuneration limit from Rs. 25,000 per month to Rs. 1 lakh per month

Issue

- Section 80JJAA of the Act allows deduction in respect of 30% of the salary of an additional employee hired during the year for a total period of 3 years. For this purpose, an additional employee is defined as one whose salary emoluments do not exceed Rs. 25,000 per month.
- Such threshold, even when introduced in 2016, was considered too low for granting any meaningful benefit. Subsequently, rising inflation and corresponding cost-of-living, have rendered the deduction almost insignificant, thereby contradicting the policy intention

of curtailing the unemployment rate in India by incentivizing hiring additional labour. The monetary limit of Rs. 25,000 per month does not provide incentive for hiring technically qualified skilled employees who provide more value addition to the business.

Recommendation

- Given the above, to keep pace with rising costs, as well as to incentivize hiring of employees in these uncertain times where the pandemic has led to severe downsizing, it is recommended to raise the threshold limit of monthly emoluments from Rs. 25,000 per month to Rs. 1 Lakh per month.

2.3 Allow deduction for Covid 19 relief expenditure incurred regardless of being classified as Corporate Social Responsibility Expenditure – Section 37

Issues

- The Indian corporate sector rose to the occasion during unprecedented Covid-19 pandemic during both waves and incurred significant expenditure for combating Covid-19 in various forms like distribution of PPE kits, masks, sanitisers, ventilators, oxygen concentrators, diversion of industrial oxygen to medical needs, free meals to poor, migrant labour and frontline warriors, free accommodation to frontline warriors in hotels, building Covid 19 hospitals, etc. Such expenditure was incurred even during unprecedented financial stress faced by corporates due to complete lockdown.
- Such expenditure faces risk of disallowance even if not classified as CSR for Companies Act purposes. This is because Explanation 2 to section 37(1) of the Income Tax Act, 1961 ('the Act') which disallows CSR expenditure refers to 'activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013" and not merely expenditure which is classified as CSR in the financial statements of the company.

Recommendation

- Hence, as a special dispensation owing to Covid-19, such expenditure may be excluded from scope of Explanation 2 to section 37(1) of the Act and allowed as a deduction whether or not it is classified as CSR for Cos Act purposes.

2.4 Allow deduction for Contribution made, Expenditure incurred towards combating COVID under Section 37 or Section 57

The Government has been swift in responding to the industry ask for clarification regarding deductions under section 80G for contribution to 'Prime Minister's Citizen Assistance and Relief in Emergency Situations Fund (PM CARES Fund)'.

As per the Press Release dated 28 March 2020, issued by the Government of India donations to PM CARES Fund will be exempted from income tax under Section 80G of the Income Tax Act, 1961 ('the Act'). Further, vide ordinance dated 31 March 2020 legislatively codified through The Taxation and Other Laws (Relaxation and Amendment of certain provisions) Act 2020 (hereinafter referred to as Amendment Act), it has been clarified by the Government that PM CARES Fund is entitled to same tax treatment as Prime Minister National Relief

Fund and therefore the contribution made to PM CARES Fund, would entitle the donor 100% deduction under Section 80G of the Act, without limitation of 10% of gross total income as provided in Section 80G(4) of the Act.

Issue

- The above is a welcome step however, companies who opt for the new regime of concessional rates of taxes (introduced vide Taxation Law Amendment Act, 2019), will not be entitled to avail deduction under Section 80G of the Act in respect of their contribution to PM CARES Fund or to any other institution (Trust/Section 25 Company/Section 8 Company, Society, Fund, Foundation) qualifying under Section 80G of the Act made after 30 June 2020.
- It is important to incentivise the taxpayers willing to contribute to protect the nation amidst economic slowdown.

Recommendations

- The government should allow full deduction in respect of the following while computing taxable income for the year in which such contribution is made or expenditure is incurred: - Any direct expenditure incurred towards combating Covid-19 crisis: and/or
- To enable the above, Sections 37 / Section 57 of the Act may be amended or notifications may be issued allowing full deduction of contribution made or expenditure incurred for Covid-19, whether it is made in cash or in kind or whether the expense is of capital or revenue in nature.
- The deduction may be allowed towards the following while computing taxable income for the year in which such contribution is made/ expenditure is incurred:
    - Contribution made to any institution (Trust/Section 25 Company/Section 8 Company, Society, Fund, Foundation) qualifying under Section 80G or registered under Section 12A/12AA of the Act;
    - Testing kits and masks for patients and health workers;
    - Equipment such as ventilators, respiratory system, personal protective gear etc.;
    - Setting up temporary treatment facilities for infected patients;
    - Training and educating general public and health workers;
    - Providing food, temporary accommodation and healthcare facilities to inter-state migrants/homeless people; and
    - Any other items/support as may be notified by the Government from time to time.
- In addition to the above, section 11 of the Act may be amended or notification may be issued to provide that the spend towards Covid-19 shall be considered as application of income for computing exemption under section 11 of the Act.

Notwithstanding anything contained in any law for the time being in force, or in its charter/ Deed/ Constitution/ Memorandum/Articles, such spend by the charitable institutions should be regarded as in compliance with the law, its Deed and Objects.

2.5 Suspend Limitation on Interest deduction for FY 2020-21 and FY 2021-22 – Section 94B

During the pandemic COVID-19, on procurement side for businesses, liquidity is severely constrained. Raising debt from local market may be comparatively challenging. Taxpayers may have to resort to tap foreign markets for borrowings (debt) which will result in accrued interest expenses.

Issue

Section 94B of the Act restricts interest expenses claimed by an entity in respect of any debt issued or guaranteed by a Non-Resident (NR) Associated Enterprise (AE) to 30% of its earnings before interest, taxes, depreciation and amortization (EBITDA) or interest payable to NR AE, whichever is less. This section does not apply to Banks, Indian Branches of Foreign Banks and Insurance Business due to special nature of their business.

Recommendation

The limitation on interest deduction should not be applicable for debts raised or guaranteed by Non-Resident (NR) Associated Enterprise (AE) during the period April 2020 – March 2021 and April 2021 – March 2022. This would result in ease of liquidity in this time of need and help taxpayers to use the amount released for business purposes.

2.6 Provide 100% depreciation for machineries, used for manufacture of ventilators, PPE Kits, Masks etc.

Issue

A huge amount of investments has put in by manufacturers of various critical medical equipment's and goods such as testing kits, masks, sanitisers etc. essential to fight and in prevention and cure of COVID-19.

It is important to incentivise the taxpayers who have made huge investments in these machineries and equipment's amidst economic slowdown.

Recommendation

It is recommended to incentivise local manufacture of critical items like ventilators, PPE, masks, etc., by granting 100% depreciation for machinery used to manufacture such items or any equipment used for combating Covid-19.

2.7 Provide extra deduction under section 80D for Mediclaim premium to cover COVID-19 treatment

Issue

COVID-19 pandemic has impacted severely not only the physical and social well-being of human beings but also had severe adverse impact in terms of slowdown of the economy coupled with increased medical expenditure. To boost the morale of the people during these critical times and to enable them cope up with the increased medial expenditure

incurred towards testing for Covid-19 infection and/or medical treatment and/or self-quarantine or home isolation, a deduction in respect of such expenditure may be allowed under the Act.

Recommendation

An extra deduction under section 80D of the Act may be granted for expenditure incurred towards testing for Covid-19 infection and/or medical treatment and/or self-quarantine or home isolation. This should be over and above the current limits under section 80D of the Act and allowed even if the individual has opted for concessional tax rates under section 115BAC of the Act and allowed to be set off against any head of income to provide more meaningful and effective relief to individuals.

Section III

Tax Rates for AOP, Issues related to TDS, TCS and Taxation of Dividend

3.1 Rationalise tax rates for Association of Person (AOP's) in infrastructure sector

Issue

- Taxation of a joint venture depends upon the agreement between the parties, forming the joint venture. If the joint venture is established in the form of a partnership firm or as a company, it is taxed accordingly i.e. as a partnership or as a company. But in all other cases, a joint venture is treated as an association of persons (AOP) or a body of individuals (BOI). From the income tax perspective, if two or more persons join hands to carry on a business but do not constitute a partnership they may be assessed as an AOP.
- In connection with infrastructure projects, a consortium of contractors is often formed to implement complex projects, particularly in Engineering, Procurement and construction ("EPC") contracts and Turnkey Projects primarily due to the requirement of expertise, and specialised resources in each specific area. The members in the consortium may or may not have clear demarcation of scope of work and they might be independent third parties or affiliated entities of a particular group.
- Leading EPC companies in India provide turnkey solutions for construction of roads, bridges, fully integrated rail & metro systems, commercial building & airports and setting up power generation plants, power transmission & distribution systems, etc. Such EPC companies have formed number of Joint Ventures in India in the form of AOP's with various partners (both overseas and local) for the purposes of bidding and execution of contracts. Such AOPs are formed for a temporary period for the specific project. In most large projects like road, rail, power, etc., the bids floated by statutory authorities have pre-condition qualification for presence of international qualified partner or presence of international partner is inevitable due to international bidding process. The AOP structure is preferred in view of relationship not constituting partnership and/or corporate form being unsuitable for short term projects.
- The Finance (No.2) Act 2019 increased the surcharge rate for Individuals, HUF, AOPs, BOIs and AOPs. From AY 2020-21, an enhanced surcharge is levied on such taxpayers as under:
    - 25 percent if taxable income is between Rs. 2 Cr to Rs. 5 Cr
    - 37 percent if taxable income exceeds Rs. 5 Cr
- Thus, the surcharge rate which was initially increased to 15 percent for AOPs vide Finance Act 2016 has been increased to 37 percent vide Union Budget 2019.
- Infrastructure is the fundamental enabler for growth. Recognising this, the government has laid down its Infrastructure Vision and Goals 2025 under which the Hon'ble Prime Minister has made a commitment of Rs 100 lakh crore under the National Infrastructure Pipeline (NIP). The investment under NIP would be made in more than 6500

infrastructure projects across sectors over the next five years. The new projects will include housing and water supply, affordable and clean energy, healthcare, airports, transportation and logistics, highways, digital services, health, education and project preparation facility for infrastructure projects to name a few.

- Further, India's vision for "Atmanirbhar Bharat" based on five significant economic pillars, includes infrastructure as one of the key pillars that will propel India towards growth with self-reliance. Several new schemes, projects and opportunities are envisioned under Atmanirbhar Bharat such as affordable housing, renewable energy, entire value chain of electricity generation (including coal mining) and distribution, to name a few. Even in the strategic sectors such as defence, space and atomic energy, participation of private and foreign sectors has been announced. Investment opportunities have also been created for agricultural infrastructure which will give a fillip to scientific storage facilities.
- The government has also taken specific measures to incentivise foreign investment. For instance, investments in notified infrastructure sectors by Sovereign Wealth Funds of foreign governments, will be allowed full tax exemption on interest, dividend and capital gains income, subject to the conditions specified.
- The thrust to infrastructure development and quality of services will lead to greater urbanisation and increased employment opportunities that, in turn, will fuel domestic demand and growth. It will also improve the ease of living and provide equitable access to infrastructure for all, thereby making growth more inclusive.
- As AOP is a preferred mode of operation for several infrastructure companies which operate in India and abroad, higher surcharge on AOPs is counter-productive and adversely dampens the efforts to attract investments in the infrastructure space through debt, equity or hybrid instruments. The increase in surcharge in an ad-hoc basis may be perceived as an uncertain tax environment by potential investors. AOP being a business entity, it seems levy of higher surcharge intended for 'super rich' taxpayers is an unintentional anomaly which needs to be corrected.
- While AOPs are taxed at base rate of maximum 30% which is same as partnership firms and LLPs, the surcharge rate differs between the two.
- The surcharge on firms/LLPs is 12% on income above Rs. 1 Cr. The surcharge rate for AOPs upto F.Y. 2018-19 was 10% for income between Rs. 50 lakh to Rs. 1 Cr and 15% for income above Rs. 1 Cr. However, from F.Y. 2019-20, the surcharge rate has been increased to 25% for income between Rs. 2 Cr to Rs. 5 Cr and 37% for income above Rs. 5 Cr
- The enhancement of surcharge on AOPs is an unintended fall out of enhancement of surcharge on individuals and HUFs. This is because AOPs are placed in same category as individuals/HUFs. While the intention was to levy higher tax on 'super rich' individuals earning more than Rs. 2 Cr in a year, it has also increased the surcharge for AOPs formed for business purposes by companies.

- As stated earlier, AOPs are formed for bidding and executing specific projects by pooling together expertise and specialised resources in specific areas by different entities. They cannot be used as vehicles for holding income generating assets. There are specific provisions regulating contribution on formation and withdrawal of assets on dissolution of AOPs to address any tax avoidance measures adopted by parties.
- Practically in majority of cases most AOPs may not be holding any asset within their fold since equipment and assets required for construction of infrastructure generally belong to individual members of AOP or may be outsourced. At best, there may be very few assets (-say, movables like machineries or vehicles) which may be held by AOP which are required to be transferred to the members on dissolution of AOP.
- From the taxation perspective, prior to the amendment in the law by Finance Act 1987, the settled legal position was that, a partnership firm/AOP is not a distinct legal entity and the partnership property in law belongs to all the partners constituting the firm/AOP, though the partnership firm /AOP may possess a tax personality distinct from the persons constituting it. Therefore, on dissolution, as the firm has no separate rights of its own in the partnership/AOP assets, there is no question of any extinguishment of the firm/AOP's rights amounting to a transfer of assets within the meaning of section 2(47) of the Act.
- However, with a view to block such escape routes for avoiding capital gains tax, Section 45(3) and Section 45(4) were inserted in the Act by Finance Act 1987 to deem pooling of assets by partners into the firm/AOP and distribution of assets by the firm/AOP to partners on dissolution or otherwise, as transfers for tax purposes, even though there would be none under the general law of partnership. The Finance Bill 2021 further rationalises these provisions by taxing settlement of capital account in cash in excess of balance in capital account (excluding revaluation)
- Moreover, the taxation rules when an AOP is dissolved is also covered by section 177 of the Income Tax Act, 1961, wherein the Income Tax Officer shall make an assessment of the total income of the association of persons as if no such discontinuance or dissolution had taken place and all the provisions of the Income tax Act, including the provisions relating to the levy of a penalty shall apply to such assessment.
- The higher surcharge rate of 37 percent leads to additional tax burden on Indian companies, which are members of the AOP formed for infrastructure projects. Therefore, it also discourages domestic companies to invest in the infrastructure sector/projects.
- Therefore, considering the requirement of the economy and the fact that infrastructure creates maximum employment in the country, the additional surcharge is a stern deterrent to the overall vision of the government to boost infrastructure as a growth vehicle to make India a self-reliant nation.

Recommendations

(i) The introduction of such high surcharge on AOPs appears to be unintentional fall out of measure to levy 'super rich' tax on rich individuals. It has discouraged investment in infrastructure projects in India which is not warranted. Therefore, we request the Government to kindly accept our request above and reduce the surcharge on AOPs to level of 10%/15% as it was prior to enhancement by Finance (No.2) Act 2019.

(ii) However, if a complete rollback is not possible, a specific carve out for infrastructure sector or relief to Indian Companies, in their capacity as member of AOP, by allowing their share of income in the AOP to be subject to surcharge rate applicable to Indian companies (i.e. 7%/12%) instead of the enhanced surcharge rate for AOPs i.e. 25%/37% may be considered.

3.2 Issues Related to TDS under section 194-0 and TCS Provisions under section 206-C of the Act

TDS under Section 194-O

Finance Act 2020 has inserted withholding tax provisions under Chapter XVII-B of the Act to cover e-commerce operators making payment to e-commerce participants (being residents). Section 194-O provides that an e-commerce operator who, through his digital or electronic platform, facilitates sale of goods or supply of services of e-commerce participant shall be liable to undertake TDS @ 1% on the gross amount of such sale or service at the time of credit or payment to e-commerce operator, whichever is earlier.

The withholding provision is not applicable while making payments to individual and Hindu Undivided Family (HUF) if the gross amount of sale or service of such e-commerce participant is Rs.5 lakhs or less and if they furnish PAN or Aadhaar to the e-commerce operator.

FA 2020 has further enhanced the scope of TCS provisions under Section 206C by introducing TCS by Travel Agents on selling overseas tour packages. As per section 206C, sub-section 1G, clause (b), seller of an overseas tour program package, who receives any amount from a buyer, being the person who purchases such package, shall, collect TCS from the buyer. The term "overseas tour program package" has been defined to mean any tour package which offers visit to a country or countries or territory or territories outside India and includes expenses for travel or hotel stay or boarding or lodging or any other expenditure of similar nature or in relation thereto.

Issues

- Both the above provisions entail serious compliance and financial challenges for the ecommerce industry and travel sector, respectively. Section 194-O of the Act has impact on working capital and cash flow for a large number of SME/MSME suppliers supplying through ecommerce operators.
- Section 206C (1G), has increased the cost of compliance and the price of tour packages sold by considerably large number of small travel agents and tour operators selling overseas tour packages.

Recommendations

- To provide a breathing space for both these industries and allow the stakeholders to focus on their survival amidst these troubled times it is recommended that section 194O and section 206C(IG) of the Act should be completely rolled back as the gains envisaged with the implementation of these provisions may not corroborate with the compliance and financial challenges caused to stakeholders.

The details of difficulties and concerns with respect to implementation of the provisions of section 194-O and section 206C(IG) of the Act is enclosed in **Annexure** to this Section.

Certain Issues with respect to Tax Collection at Source under section 206C(IH)

(a) In case of sales by consignment agent on behalf of principal, it may be clarified that obligation to collect TCS shall be on Principal

Amendment by FA 2020

- Section 206C(1H) requires every person being seller to collect TCS from the buyer of goods on receipt of sale consideration exceeding in aggregate Rs. 50Lakh in any previous year. The section excludes particular class of persons from the scope of buyer and seller.

Issue

- The provision of section 206C(1H) provides that every person being a seller shall collect TCS from the buyer. In case of sales by consignment agent on behalf of principal, question may arise whether TCS obligation is on the principal (who is the legal seller) or the agent who receives sales consideration from the buyer.

Recommendations

- It may be clarified that the legal obligation to collect TCS is on Principal and not on the agent undertaking sales activity on behalf of Principal. Hence the primary obligation to comply with TCS is on the principal being the legal seller of goods.

  But since, practically, the sales consideration is first received by the agent, it may also be clarified that where agent collects TCS from the buyer and deposits with Government using his own TAN and issues TCS certificate to the buyer, there shall be no adverse consequences for principal for non-collection of TCS.

- It may also be clarified that credit of TCS to the buyer would be available in all cases even in case where the TCS is collected by agent and not the principal on whose behalf sales are undertaken.

(b) Carve out B2B transactions from the ambit of TCS provision under section 206C(1H)

In order to widen and deepen the tax net, FA 2020 extended the TCS provisions to cover a seller of "goods" other than the goods exported outside India or goods specified under section 206C(1)/ (1F)/ (1G) of the Act such as alcohol, motor vehicles, forest produce, scrap etc.

The provision is applicable w.e.f. 1 October 2020. TCS provisions would apply only to a seller whose sales, turnover or gross receipts in the business carried on by him exceeds INR 10 Crores during the immediately preceding financial year, and who receives, in any previous year, any amount as consideration for sale of goods aggregating to Rs. 50 Lakh or more, from a single buyer.

Further, the definition of 'buyer' excludes from its scope Central Government, State Government, various other authorities, person importing goods into India and also empowers the Central Government to notify class of persons for further exclusion.

Issue

- The provisions of TCS for sale of goods under section 206C(1H) do not specifically make distinction between sales made to the intermediate customers (B2B transactions) and sales made to the final customers (B2C transactions). In absence of specific exclusion for B2B transactions, the provision appears to apply for all types of sale transactions, irrespective of whether the transaction involves sales to intermediate entities/ customers or it is sale to final customers.
- Applicability of TCS provisions to B2B transactions as well may result in tax being collected at multiple levels, in turn, may lead to cash blockage at entity level. In a supply chain structure consisting of manifold entities (as is usually prevalent in the retail sector), this would result in tax being collected multiple times on the same transaction. Collection of tax at multiple entity levels increases the administrative compliance burden, transaction costs and results in cash flow trap. Since B2B transactions are made with multiple vendors, it is administratively burdensome to apply for lower/ NIL TCS for all vendors. Further, benefit of lower/ Nil TCS has not been extended to section 206C(1H) by FA 2020.

  Further, such transactions being subject to GST, there is already an audit trail available with the GST Department which can be easily leveraged by the Income tax Department through electronic sharing of data on automated basis and making use of Artificial Intelligence to mine the data to detect tax evasion. TCS on sales results in multiple levy of tax on same transaction.

Recommendation

- It is recommended to provide exclusion for sellers from collection of tax under section 206C(1H) selling goods to intermediate persons/dealers (B2B transactions). Alternatively, since the information pertaining to GST registered dealers is already available with the Government, the TCS may be made applicable only to buyers who are not registered with GST.

(c) Clarify the scope of the term "goods" used in section 206C(1H)

FA 2020 extended the TCS provisions to cover a seller of "goods" other than the goods exported outside India or goods specified under section 206C(1)/ (1F)/ (1G) of ITA such as alcohol, motor vehicles, forest produce, scrap etc.

Issue

- Section 206C(1H) triggers TCS on sale of all goods except goods which are being exported outside India or goods covered by other TCS provisions of section 206C(1)/ (1F)/ (1G) such as tendu leaves, alcohol, motor vehicles etc. The term "goods" covered by section 206C(1H) is not defined in the Act which creates ambiguity on scope of the said TCS provision.
- It is also not clear whether the definition of goods needs to be interpreted as per the Sale of Goods Act 1930 (SOGA) or the Central Goods and Services Tax Act 2017 (CGST Act) or some other legislation. For instance, whether the term "goods" includes shares, securities, money/ foreign currency, electricity etc. within its scope is not clear since there are different inclusions and exclusions within scope of 'goods' under various laws. For instance, definition of goods under SOGA includes stock and shares but definition of goods under CGST Act excludes securities.
- The CBDT Circular No. 17/2020 has clarified that TCS will not apply to transactions carried out through stock exchange and power exchange. However, this raises ambiguity for off-market transactions in such items as also transactions in actionable claims, foreign currency, etc.
- Clarity on these items is very crucial to banking and financial sector. If TCS is considered to be applicable to these items, it will have huge compliance and cash flow burden for the industry. The banks will need to collect TCS on all foreign remittances (since these involve sale of foreign currency by banks to remitters). Similarly, beneficiaries of inward remittances like exporters, companies raising equity and debt from overseas, etc. will need to collect TCS on all foreign inward remittances from the banks (since these involve sale of foreign currency by beneficiaries to banks).
- Also, the Government's stated position is that sale of computer software is income in the nature of 'royalty' attracting TDS under section 195 or 194J of the Act. To avoid cascading impact of TDS at multiple levels in the chain, the CBDT has notified software payments to be exempt from TDS under section 197A(1F) where tax is already deducted at the first level under section 195 or 194J (Refer Notification No.21/2012 dated 13 June 2012). Consistent therewith, it is suggested that CBDT may also clarify that sale of computer software will not attract TCS on sale of goods.

Recommendation

It is therefore recommended that the term "goods" should be defined clearly in the ITA for the purpose of TCS under section 206C(1H) and it should specifically exclude items such as shares, securities, actionable claims, money/ foreign currency etc. from its scope.

(d) Clarify adjustment of amounts representing sales return, discounts, rebates, price adjustments or other credit notes from subsequent receipts while applying TCS

Amendment by Finance Act, 2020

Section 206(1H) as amended by FA 2020, provides for TDS collection by seller who receives, in any previous year, any amount as consideration for sale of goods aggregating to Rs. 50 lakh or more, at the time of "receipt" of such sales consideration exceeding Rs. 50 lakhs.

Issue

Para 4.6 of Circular 17/2020 clarifies that no adjustment on account of sales return, discount or indirect taxes including GST is required to be made since TCS collection is made with reference to receipt of amount of sale consideration.

This clarification has created some amount of confusion for the industry. We believe that Circular tries to clarify that since the TCS is applicable on receipt of consideration, if such payment is received by seller after deducting sales returns, discount, etc. no further adjustment is required since TCS is to be paid on the net amount received by the seller. This point requires elucidation with an example as provided in para 4.2.2 of the Circular in respect of payment gateways.

Recommendation

The clarification provided at para 4.6 of Circular No. 17/2020 may be appropriately explained with the help of example to clear any confusion.

(e) Extend benefit of lower TCS rate to remittances for medical treatment similar to benefit granted for remittances out of education loan

As per the amendment by FA 2020 to section 206C(1G)(a), Authorised Dealer (AD) is not required to collect TCS where the amount or aggregate amount of remittances outside India under LRS, other than for purchase of overseas tour package, is less than Rs. 7 Lakh in a FY. Further, TCS is required to be collected at the rate of 5% on the amount which is in excess of Rs. 7 Lakh.

However, in case where the remittance is out of the loan obtained from any financial institution (as defined in section 80E of the Act) for the purpose of pursuing any education, AD is liable to collect TCS at the rate of 0.5% (instead of 5%) on the amount or aggregate of the amounts in excess of Rs. 7 Lakh remitted by the buyer in a financial year. This beneficial provision was introduced during the enactment stage of FB 2020.

Issue

Amendment providing for lower rate of TCS @ 0.5% on remittances out of education loan availed from a qualifying financial institution is a welcome move by the Government. However, considering the importance of education and medical sectors, it is not clear why similar benefit is not extended to remittances made for medical expenses/assistance, subject to suitable safeguards as the Government may impose.

In many cases, remittances are made to foreign hospital for advanced medical treatment. Just as in case of foreign education, the remittance is made for genuine purpose. Imposing TCS at high rate of 5% results in cash trap for the remitter at a time he is facing distress due to medical emergency. In fact, it is a better case for lower TCS on unplanned expenditure than foreign education which is a planned expenditure.

Recommendation

Considering the importance of education and medical sectors, it is recommended that the TCS provisions should not apply in case of remittances made outside India under LRS for

study/ education abroad or for availing medical treatment or incurring medical expenses abroad, with suitable safeguards as the Government may deem fit.

Alternatively, akin to lower rate of TCS for remittances out of education loan, benefit of lower TCS rate @ 0.5% should also be extended for remittances made in relation to medical expenses/ relief.

(f) Extend relaxation of provisions for assessee-in-default to sub-sections (1F)/(1G)/(1H) of section 206C

Section 206C(6A) of the Act provides that if the person responsible for collecting tax (say, seller) does not collect whole or part of the tax amount or fails to pay after collecting, he shall be deemed to be an assessee-in-default.

The proviso to section 206C(6A) provides that such person/seller responsible for collecting tax under section 206C shall not be deemed to be assessee-in-default if the buyer has:

- Furnished his return of income under section 139(1)
- Taken into such amount (on which TCS was collectible) for computing income in his return of income, and
- Paid tax due on income declared by him in the return of income

Amendment by FA 2020

FA 2020 has restricted the benefit of the above proviso only to sub-section (1) and (1C) of section 206C of the Act. In other words, the relaxation has not been extended to expanded scope of TCS such as sub-section (1F)/(1G)/(1H) of section 206C of the Act in relation to sale of motor cars, LRS, overseas tour program package and sale of goods.

Issue

The underlying rationale of proviso to section 206C(6A) is statutory recognition of legal position clarified by CBDT vide its Circular No. 275 dated 29 Jan 1997 upheld by Supreme Court in the case of Hindustan Coca Cola Beverages (P) Ltd v. CIT (293 ITR 226) and Ely Lilly & Co(I) Pvt. Ltd (312 ITR 225) viz. once the payee/buyer has paid tax and filed return, the purpose of TDS/TCS of ensuring tax collection is achieved and hence, the payer/seller should no more be considered as an assessee-in-default. Hence, the rationale of not extending the relaxation granted by the proviso to other sub-sections is not clear. In case where the buyer has already done the compliance as stated in the proviso to section 206C(6A), not extending the benefit to the sellers/persons responsible for collecting tax under section 206C(1F)/(1G)/(1H) will lead to double whammy and create unnecessary administrative and tax compliances for the seller/ buyer.

Recommendation

It is recommended that the relaxation provided by the proviso to section 206C(6A) may be extended to the other provisions of TCS such as sub-section (1F)/(1G)/(1H) of section 206C also, since once the buyer has already done the necessary compliance, not extending the

benefit of the proviso will lead to double whammy and create unnecessary administrative and tax compliances for the seller/ buyer.

(g) Extend benefit of lower/ NIL tax collection certificate under section 206C(9) to TCS on LRS remittances, overseas tour package, sale of goods and motor vehicles

Section 206C(9) provides for collection of tax at lower rate as against relevant rate provided in the respective sub-section (1) of section 206C for items such as alcohol, scrap etc. or subsection (1C) of section 206C for items such as parking lot, toll plaza etc. in case where the Assessing Officer is satisfied that the total income of the buyer/ licensee justifies collection of tax at a lower rate. Such certificate remains valid till the time it is cancelled by the Assessing Officer.

Amendment by FA 2020

In order to widen and deepen the tax net, the FA 2020 extended the TCS obligation to authorised dealers who receive money for remittance outside under LRS under section 206C(1G)(a) and to sellers of overseas tour package under section 206C(1G)(b). In both the cases, TCS applies at the rate of 5% at the time of receipt or debit whichever is earlier, and in case of no PAN/ Aadhaar, the TCS rate is increased to 10%. Further, it is also not extended to sale of goods by section 206C(1H).

Issue

The benefit of availing lower tax collection certificate as provided for transactions covered under section 206C(1)/(1C) is neither provided in sub-section (1G)/(1H) nor sub-section (9) of section 206C. The policy rationale for non-extension of lower TCS benefit to transactions of LRS, overseas tour package and sale of goods as distinguished from other TCS provisions is not clear. Further, apart from the above newly introduced provisions, such benefit is also not extended to section 206C(1F) dealing with TCS on sale of motor vehicles.

Recommendation

It is recommended that the benefit of availing lower tax certificate may also be extended to TCS under section 206C(1G) charged @ 5% on remittances outside India through LRS and overseas tour package, TCS under section 206C(1H) on sale of goods as also under section 206C(1F) on sale of motor vehicles.

3.3 Provide clarity with respect to TDS provisions on cash withdrawals under section 194N

Finance (No. 2) Act, 2019 inserted section 194N in the Act providing for withholding of tax by a bank (including a co-operative bank) or a post-office, where the aggregate withdrawals in cash in a year exceeds Rs. 1 Crore. Such deduction is to be carried out at 2% on the amount of withdrawal in cash exceeding Rs. 1 Crore.

Section 194N of the Act as inserted, read as follows: *Every person, being, —*

(a) banking company to which the Banking Regulation Act, 1949 (10 of 1949) applies (including any bank or banking institution referred to in section 51 of that Act).

(b) *a co-operative society engaged in carrying on the business of banking; or*

(c) *a post office, who is responsible for paying any sum, or, as the case may be, aggregate of sums, in cash, in excess of one crore rupees during the previous year, to any person (herein referred to as the recipient) from one or more accounts maintained by the recipient with it shall, at the time of payment of such sum, deducts an amount equal to two per cent of **sum exceeding one crore rupees**, as income-tax"*

Amendment by FA 2020

FA 2020 substitutes the existing section 194N with a revised provision. The newly inserted section 194N now reads as follows:

''194N. Every person, being, —

(d) *a banking company to which the Banking Regulation Act, 1949 applies (including any bank or banking institution referred to in section 51 of that Act).*

(e) *a co-operative society engaged in carrying on the business of banking; or*

(f) *a post office, who is responsible for paying any sum, being the amount or the aggregate of amounts, as the case may be, in cash exceeding one crore rupees during the previous year, to any person (herein referred to as the recipient) from one or more accounts maintained by the recipient with it shall, at the time of payment of **such** sum, deduct an amount equal to two per cent of **such** sum, as income-tax:"*

In addition, a new first proviso has been inserted to provide a lower threshold of cash withdrawals in case of specified Taxpayers. The first proviso reads as follows:

*Provided that in case of a recipient who has not filed the returns of income for all of the three assessment years relevant to the **three previous years, for which the time limit of file return of income under sub-section (1) of section 139 has expired, immediately preceding the previous year in which the payment of the sum is made to him,** the provision of this section shall apply with the modification that—*

(i) *the sum shall be the amount or the aggregate of amounts, as the case may be, in cash exceeding twenty lakh rupees during the previous year; and*

(ii) *the deduction shall be—*

- *an amount equal to two per cent of the sum where the amount or aggregate of amounts, as the case may be, being paid in cash exceeds twenty lakh rupees during the previous year but does not exceed one crore rupees; or*
- *an amount equal to five per cent. of the sum where the amount or aggregate of amounts, as the case may be, being paid in cash exceeds one crore rupees during the previous year.*

Issue

The newly substituted S. 194N is ambiguously worded. The phrase "sum exceeding one crore rupees" which existed in the erstwhile provision has been deleted and hence it gives rise to an ambiguity of whether deduction of tax needs to be made only on the sum exceeding Rs. 1 Crore or on the entire amount of withdrawal inclusive of Rs. 1 Crore.

The intent of the amendment does not appear to be to change the existing provisions but merely to provide a lower threshold for specified Taxpayers. In fact, in case of cash withdrawals by specified Taxpayers, the first proviso clearly indicates that the withholding would apply only on withdrawals exceeding INR 20 lakhs.

The determination of three years for which the return filing compliance needs to be checked for applicability of the lower threshold prescribed in first proviso.

Further, the newly introduced first proviso can result in more than one interpretation on which of the three years are to be considered for the purpose of determining the applicability of the lower threshold. The two possible interpretations of the first proviso are as follows:

- View 1: Three years refer to the three financial years (FY) immediately preceding the year for which the due date for filing return of income under section 139(1) of the Act has already expired as on the first day of year in which cash withdrawal is made. For e.g. For cash withdrawals in the year FY 2021-22, the three years in which the compliance of return filing is to be checked for would be FY 2017-18, 2018-19 and 2019-20 (i.e. AY 2018-19, AY 2019-20 and 2020-21).
- View 2: Three years refer to the three financial years immediately preceding the year for which the due date for filing Return of Income (ROI) has expired as on the date of cash withdrawal. Since the applicability of lower threshold depends on filing of return of income in such three years, withholding in FY 2021-22 would be a rolling period. For instance, consider a case where the person who is withdrawing cash is an individual. In the case of an individual, the return filing due date u/s 139(1) falls on 31 July 2021. Thus, for withdrawals till 31 July 2021, the three years would be FY 2017-18, 2018-19 and 2019-20 (i.e. AY 2018-19, AY 2019-20 and AY 2020-21). Subsequent to 31 July 2021, the three years would be FY 2018-19, 2019-20 and 2020-21 (i.e. AY 2019-20, 2020-21 and 2021-22).
- The CBDT has provided a functionality on the income tax department's website for verifying an assessee's return filing compliance for 3 years for the purposes of determining the correct rate of TDS under section 194N of the Act. However, the result of the process does not indicate PAN and name of the assessee which can be stored by the bank as an evidence of verification of assesee's return filing status for future verification.

Recommendations

- It is recommended that either the language of section 194N is replaced with the erstwhile language or a circular be issued to clarify that the withholding would apply only in respect of withdrawals exceeding Rs 1 Crore in case of non-specified Taxpayers.
- It may be clarified that View 1 as described above i.e. a fixed period of three financial years for which the return filing due date under section 139(1) has expired prior to commencement of the relevant financial year in which cash is withdrawn, is to be considered for the purpose of determination of applicability of the lower threshold under the first proviso. This will provide ease of compliance and certainty for the banks for applying the lower threshold throughout the financial year and avoid complications of position of applicability of first proviso changing in the middle of the year.

3.4 Ambiguities pertaining to Dividend

(a) Dividend surcharge mismatch for different classes of non-resident taxpayers and mismatch with income from mutual funds and units of business trusts

Issue

The amendments at enactment stage to FB 2020 have reduced surcharge rates on dividend for individuals, HUFs, AOP, BOI and AJP to maximum 15% (as compared to highest surcharge of 37%) as per original budget proposal. The amendments carried out to FB 2020 at enactment stage are at Parts II and Part III of First Schedule to FB 2020 which are linked to 'rates in force' referred in section 2(5) of FB 2020. Thus, wherever the relevant final rate or TDS provision refers to 'rates in force', the maximum surcharge on dividends stands reduced to 15%.

However, many final rate and TDS provisions provide for specific rates of tax on dividend income. They are covered by section 2(6) and section 2(9) of FB 2020. Unfortunately, section 2(6) and section 2(9) of FB 2020 have not been amended at enactment stage to reduce maximum surcharge to 15% for dividend income. The Taxation and Other Laws (Relaxation and Amendment of certain provisions) Act 2020 has extended the relief from higher surcharge on dividends to Foreign Portfolio Investors (FPIs). However similar relief has not been extended to any other class of non-resident investors. This has resulted in mismatch between (a) surcharge on dividends between different classes of non-resident taxpayers and (b) TDS rates and final rates on dividend income for some non-resident taxpayers. This is summarised in Table given below.

Recommendation

It is suggested that CBDT may clarify whether the mismatches are intentional. If they are unintentional, CBDT may clarify how they shall be addressed through legislative amendments and what rates can be adopted by taxpayers in the intervening period.

Table summarising dividend surcharge rate mismatch for different classes of non-resident taxpayers.

Section	Nature of payment to non-resident	TDS rate prescribed (rates in force or specified rate)	Whether covered by s.2(5) r.w Part II of First Schedule or s.2(6) of Finance Bill 2020?	Whether TDS at higher or lower surcharge?	Whether final tax liability for advance tax purposes at higher or lower surcharge?
194LBA	Dividend income from business trust	Rate specified - section 194LBA(2) – 10%	s. 2(6) of Finance Act, 2020	Higher surcharge	Higher surcharge Rate – 20% S.115A(1)(a)(i) r.w. clause (a) of third proviso to s.2(9) of Finance Act 2020
194LBB	Dividend income from Alternative Investment Fund	Rates in force - section 194LBB(ii)	s. 2(5) of Finance Act, 2020	Lower surcharge	Higher surcharge S.115A(1)(a)(i)r.w. clause (a) of third proviso to s.2(9) of Finance Act 2020
194LBC	Dividend income from Securitisation Trust (Practically possibility of dividend from securitisation trust is less likely but cannot be completely ruled out)	Rates in force - section 194LBC(2)	s. 2(5) of Finance Act, 2020	Lower surcharge	Higher surcharge S.115A(1)(a)(i)r.w. clause (a) of third proviso to s.2(9) of Finance Act 2020

195	Dividend income	Rates in force	s. 2(5) of Finance Act, 2020	Lower surcharge	Higher surcharge S.115A(1)(a)(i)r.w. clause (a) of third proviso to s.2(9) of Finance Act 2020

(b) Dividend vs. mutual fund income & income from units of business trusts (ReITs/InvITs)

Issue

While maximum surcharge on dividend income is reduced to 15%, there is no corresponding reduction in surcharge for income from mutual fund units and units of business trusts (REIT/Invits). This creates mismatch between different classes of capital market equity instruments. It may be noted that the capital gains income from equity oriented mutual funds and units of business trust are subjected to lower surcharge up to 15%. Similarly, there should be parity between surcharge on dividend income and income from mutual fund units/units of business trust.

Recommendation

Income from mutual funds and business trusts may be put at par with dividend income by restricting maximum surcharge to 15%.

(c) Clarify person whose PAN should be considered in case of dividend payment on GDRs
Issue

The TDS rate on dividend payment on GDR is 10% u/s. 196C. Following extracts from the erstwhile Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depositary Receipt Mechanism) Scheme, 1993 made it clear that dividend paying company can rely on PAN of overseas depository for making TDS compliance in India "Taxation on shares issued under Global Depositary Receipt Mechanism.

9. (1) Under the provisions of the Income-tax Act, income by way of dividend on shares will be taxed at the rate of 10 per cent. The issuing company shall transfer the dividend payments net after deduct tax at source to the Overseas Depositary Bank.

(2) On receipt of these payments of dividend after taxation, the Overseas Depositary Bank shall distribute them to the non-resident investors proportionate to their holdings of Global Depositary Receipts evidencing the relevant shares. The holders of the Depositary Receipts may take credit of the tax deducted at source on the basis of the certification by the Overseas Depositary Bank, if permitted by the country of their residence."

Similar provision is not present in extant Depository Receipts Scheme, 2014. The issue was not relevant earlier since dividend was exempt under section 10(34). But now since dividend

income is taxable in hands of shareholder, issue will arise in whose PAN is the dividend paying company supposed to do TDS compliance in India such that provisions of section 206AA requiring higher TDS @ 20% are not triggered.

Recommendation

It may be clarified through a Circular or through express amendment in section 206AA or section 196C, that TDS compliance on dividend payment on GDRs will need to be made under PAN of overseas depository.

3.5 Issues - Classical system of dividend taxation

(a) Allow entire expenditure incurred to earn dividend income or at least, remove the restriction on allowability of interest expenditure only upto 20% of dividend income – Section 57

Under the classical system of dividend taxation introduced by the Finance Act, 2020, wherein the dividend income would be taxed only in the hands of shareholders and the distributing company would not be subjected to DDT. The taxation of dividend in the hands of shareholders would take place at their corporate tax rate or slab rates (which could be as high as 42.74%) or tax rate applicable to such dividend income, as the case may be.

However, no deduction of any expenditure is permitted against dividend income except 20% of the interest expenditure.

Issues

- Since the entire dividend income is taxable in the hands of shareholder, the corresponding expenditure incurred by such shareholder to earn such dividend income should also be allowed as deduction. The taxation of dividend income under the head "Income from other Sources" (IFOS) should take place exactly in the manner similar to taxation of other nature of income under the head "IFOS". For the other income which is taxed under IFOS, Section 57(iii) grants deduction of entire expenditure incurred to earn such income.
- Under the current regime of dividend taxation, no deduction of any expenditure is permitted against dividend income except 20% of the interest expenditure. Thus, to put it differently, any expenditure (other than interest) incurred to earn dividend income is fully disallowed and only interest expenditure is allowed which is also capped at 20% of dividend income which is offered to tax under "total income". This may unnecessarily increase the finance cost of the investor who mainly invest in equity shares by borrowing the money from banks/ financial institutions/ third party lender.
- This may lead to huge financial burden for the taxpayers since they would be statutorily required to disallow the genuine and bonafide expenditure incurred to earn such dividend income which is taxable at full rate under the head Income from other Sources.
- Further, it may be noted that interest burden of the investors would be fixed till the time borrowings are not repaid. However, the dividend income is not constant and is at complete discretion of the domestic investee companies. Hence, there may arise a

situation wherein no dividend income is earned, but huge interest expenditure is incurred by the investors which will be disallowed as per the amendment in absence of dividend income being part of total income. Moreover, in the year when dividend income is earned, the proviso to section 57 further restricts the claim of deduction merely to 20% of dividend income included in total income. This would lead to harsh consequences on investors who would have invested by taking huge loans.

- Further, many acquisitions take place pursuant to proceedings of Insolvency and Bankruptcy Code, 2016 (IBC). In order to revive the IBC acquired company, huge funds are required to be infused by shareholder in the acquired company. Such infusion of funds may take place in the form of equity and funds may be arranged by parent shareholder by obtaining loan. Thus, there would be huge interest burden on parent shareholder which has taken initiative to revive the underlying company pursuant to insolvency proceedings. Such interest which is genuine commercial cost could also be subject matter of disallowance due to proviso to section 57 of the Act.
- Even if the taxpayer is incurring a commercial loss on the investment transaction (on account of high interest expenditure), it will be required to pay tax on gross dividend income. Such taxation of notional dividend income will not align with the real income theory of taxation.

Recommendations

- It is recommended that similar to section 57(iii), any expenditure which is wholly and exclusively incurred to earn such dividend income should be fully allowed as deduction. This is because similar to other income taxed under Income from other Sources, even dividend income should be taxed in same manner and consequently, the expenditure incurred to earn such dividend should also be given same treatment of being fully allowable as deduction.
- In a scenario where it is not agreeable to allow all the expenditure incurred to earn such dividend income, the entire interest expenditure may be allowed as deduction instead of current provision of restricting it to mere 20% of the dividend income included in the total income.

(b) Ambiguity with regard to use of phrase "total income" under proviso to Section 57 which allows interest deduction only if dividend income is included in "total income" For ready reference, the language of proviso to section 57 is reproduced as under:

> *" Provided that no deduction shall be allowed from the dividend income, or income in respect of units of a Mutual Fund specified under clause (23D) of section 10 or income in respect of units from a specified company defined in the Explanation to clause (35) of Section 10, other than deduction on account of interest expense, and in any previous year such deduction shall not exceed twenty percent of the dividend income, or income in respect of units, **included in** **the total income for that year**, without deduction under this section."*

Issues

- The above language suggests that interest expenditure would be allowable to the extent of 20% of dividend income which is included in “total income” of the respective financial year.
- Section 80M deduction is one of the deductions in the determination of total income. The total income is determined after adjusting deductions admissible under Chapter VIA, including section 80M of the Act.
- The reference to “total income” may, therefore, be misinterpreted to suggest that the 20% expense limit should be applied to net dividend amount, after adjusting rollover deduction admissible under section 80M of the Act.
- The legislative intent seems to be to grant deduction of an amount up to 20% of gross dividend receipt; and Section 80M deduction should be adjusted from the net dividend income which would otherwise have been chargeable to tax.

Recommendation

- It is recommended to remove the phrase “included in the total income for that year” as currently under proviso to section 57 of the Act. This would ensure that deduction for interest expenditure is correctly allowed up to 20% of “gross dividend receipt” and not of net dividend amount which is derived after adjusting rollover deduction admissible under section 80M of the Act.

(c) Allow small shareholder deduction for dividend income upto certain threshold, as may be determined

It is recommended that akin to provisions of section 80L of the Act prevailing in statute at the time of classical dividend taxation system of FY 2002-2003, deduction upto certain threshold be granted (say upto Rs. 25000) if gross total income of any taxpayer includes dividend income.

(d) Rationalize deduction under Section 80M

Finance Act 2020 abolished payment of Dividend Distribution Tax (DDT) by companies by replacing it with the classic system of taxing dividend in the hands of shareholders. Simultaneously section 80M of Income Tax Act, 1961 has been re-introduced to provide deduction to such companies from the Gross Total Income (GTI) equivalent to lower of dividend received or dividend distributed to its shareholders.

However, the legislature seems to have not envisaged the situation, where GTI of a company is negative or Nil even after the receipt of dividend from the company in which such company has made investment. This could be due to current year business losses or brought forward unabsorbed depreciation being higher than the dividend received and thus even though such company would have declared dividend to its shareholders, it will still not be eligible to claim deduction under section 80M of the Act. In other words, any amount of deduction under this section is available only when the GTI is positive.

It may be noted that a company is permitted to distribute dividend under Companies Act based on quantum of its ‘distributable profits’ which can be materially different from its taxable profits in view of incentives, deductions and set off of losses under tax laws. Hence, it is likely that a company may distribute dividend based on its book profits even though it has NIL taxable income due to set off of losses.

Thus, on the same dividend income, while on one hand the loss making domestic co’s current year business losses or unabsorbed depreciation will get reduced after set off against dividend income and on the other, the shareholders shall be liable to pay tax on the dividend income, thus effectively resulting into a double taxation situation. This may not be in line with intention of the legislature of providing relief from cascading impact of taxing inter-corporate dividend whereby benefit of deduction is given by presuming that such distribution is first made out of the dividend received by the company and thus to the extent dividends are further distributed, the company is deemed to be a fiscally transparent entity through which the dividend received by it passes and reaches in the hands of ultimate shareholders where it is sought to be taxed.

It is highlighted that even in earlier DDT regime, a similar benefit was available to the companies vide section 115-O(1A) of the Act whereby dividend from subsidiary company as prescribed therein received by a domestic company was allowed as reduction for determining the net amount on which DDT was to be paid by the company without any condition of GTI being positive or negative. However, it seems that in the current regime, a similar provision has been missed out, thus causing unintended hardship for such companies.

It is recommended that all companies which have distributed/paid dividend to its shareholders should also be eligible to claim deduction under section 80M of the Act. The scheme of taxation for dividend should be amended such that only the net dividend income i.e. after reducing the dividend paid forms part of Gross Total Income. This will ensure that the cascading effect and consequential double taxation of dividend income is mitigated and the company which declares dividend is able to carry forward the full amount of current year losses or brought forward unabsorbed depreciation. This will be consistent with the object of section 80M of the Act.

Further, inter-company dividends are eligible for deduction under section 80M of the Act but still taxable for MAT purpose and will generate MAT credit which is not the intention of this section after abolishment of DDT provision. It is accordingly recommended that inter-company dividends eligible for 80M deduction should be treated as exempt for the purpose of MAT calculation.

3.6 Reduce TDS rate for “fees for professional services” at par with prescribed rate under section 194C

The Finance Act, 2020 has reduced the TDS rate under section 194J to 2% (from existing 10%) in case of FTS payments.

The Explanatory memorandum to the Finance Bill, 2020 provides that the amendment is proposed since there are large number of litigations on the issue of short deduction arising out of characterization dispute between section 194C and section 194J of the Act.

Issue

While provision of 2% rate for FTS payments is a welcome change, the amendment will give rise to a new litigation in the form of distinction between professional services and technical service. Thus, such selective amendment for providing lower rate only for FTS payments is in direct conflict with the rationale in the Explanatory Memorandum that it is intended to avoid litigation on short deduction issues.

Further, without prejudice, the issue persists in case of individual and HUF as TDS rate for individual and HUF under section 194C of the Act is 1% while the rate of TDS under section 194J of the Act is 2%.

Recommendations

- It is recommended that the TDS rate in case of "fees for professional services" under section 194J should also be reduced at par with rate provided under section 194C to achieve true parity and avoid further litigation on professional services v. technical services (FTS). In the alternative, "professional services" should be defined to be restricted to regulated professions.
- Without prejudice to the above, since the intent is to reduce characterisation dispute between TDS under section 194C v. 194J, the TDS rate under section 194J should be kept at par with section 194C in respect of individual and HUF i.e. 1% TDS rate for individual and HUF under section 194J of the Act as well.

Annexure

Issues and Recommendations pertaining to Section 194-O and Section 206-C of the Income Tax Act, 1961 ('the Act') as introduced in the Finance Act, 2020

A. Section 194-O: Coverage of e-commerce operator

1. Exclude such platforms from scope of e-commerce operator which merely provide list and information of products but does not enable sale of such products

Amendment by FA 2020

- S.194-O requires an e-commerce operator to withhold taxes on transaction of sale or service that is facilitated by such e-commerce operator.

Issue

- There are some digital platforms which merely allow sellers to list their products and their contact information of the portal and potential buyers to solely view such product information. Thereafter, the role of the platform ends. If the buyer is interested, he can contact the seller with the contact details provided but all communications/ negotiations and completion of sale happens offline between buyer and seller. The platform is not even aware whether or not sale has taken place. In other words, such platforms merely act as classified repositories.
- However, owing to the wide meaning of the term "facilitate", doubts may arise whether such platform which act as classified repositories and have no role to play in completion of sale or service will also be obligated to withhold under S. 194-O.

Recommendations

- It is recommended that such e-commerce operators which merely provide for listing of price, referrals, product, information should be excluded from scope of S.194-O

2. E-commerce operator be liable for TDS only when payment is routed through such e- commerce operator

Amendment by FA 2020

- S.194-O requires that the e-commerce operator to withhold tax on payment or credit of amount of sale or service to e-commerce participant. Further, Explanation to Section 194-O(1) deems that direct payment made by customer to e-commerce participants for sale of goods or services is deemed to be amount paid or payable by

e-commerce operator to e-commerce participants. Also, S.194-O(6) provides that the e-commerce operator shall deemed to be a person responsible for paying to the e- commerce participants.

Issue

- In certain types of electronic commerce transactions, where the sale of goods or provision of service takes place directly between buyer and seller, the e-commerce operator does not have visibility over the transaction. In such cases, the e-commerce operator may not be aware of the pricing of the goods, conclusion of the contract, etc.
- Also, there are numerous e-commerce models or aggregators where e-commerce operators are not contractually obliged to collect or pay the transaction amounts or at times even involved in conclusion of transaction. In fact, the suppliers/ participants are required to make commission payments to such platforms
- Levying TDS obligation on such e-commerce models not only creates difficulty in deducting TDS in absence of payments but also adds to administrative inconvenience and working capital hurdles. It casts an unnecessary obligation on platforms who are not involved in consummation of the transaction between buyer and the seller. This is completely against the philosophy of TDS obligations which otherwise arise only on payments or credits to the contracting party.
- Even GST law also imposes a Tax Collected at Source ('TCS') of 1% on e-commerce operators from the consideration received by it on behalf of a supplier of goods or services through its online platform. In other words, there is no GST TCS obligation where the sale consideration is not routed through the e-commerce operator.

Recommendation

- Appropriate clarifications or guidelines may be issued to clarify that where the transactions which are strictly between the end-user/customer and e-commerce participant and where no payment is ever due from the e-commerce operator to the ecommerce participant, such transaction will not be covered within the scope of S.194-O.
- Alternatively, it may be clarified that TDS obligation will extend to only such transactions where customer has a choice to either pay through e-commerce operator or directly to e-commerce participant and e-commerce operator holds information of consummation of transaction between customer and e-commerce participant (eg. radio cab service).

3. Clarify that S. 194-O does not apply in scenarios where e-commerce operator is selling own goods on its own platform Amendment by FA 2020:

- S.194-O requires an e-commerce operator to withhold taxes on transaction of sale or service of e-commerce participant that is facilitated by such e-commerce operator.

Issue:

- Considering various e-commerce models, it is possible that businesses operate online stores in India i.e. sellers are selling own goods through its own website. It may be noted that though the sale may qualify as electronic commerce, the e- commerce operator and e-commerce participant shall be the same person. In other words, the sale is not facilitated by a third party.
- However, since the sale is facilitated by a digital platform, doubt may arise whether such transaction is covered under Section 194-O of the Act.

Recommendation:

- It may be clarified that such cases where the seller is selling his own goods or services on its own platform is outside scope of Section 194-O of the Act.
- GST law imposes a TCS of 1% on e-commerce operators from the consideration received by it on behalf of a supplier of goods or services through its online platform. Further, ecommerce operators are also required to obtain separate GST registration certification. Considering the definition of e-commerce operator under GST laws and S. 194-O is the same, the Act may consider applying S. 194-O only to such players who are registered "e-commerce operator" under GST laws.

4. Clarification on person liable to withhold tax where multiple e-commerce operators are involved in the transaction chain

Amendment by FA 2020

- S. 194-O requires an e-commerce operator to withhold taxes on transaction of sale or service that is facilitated by such e-commerce operator.

Issues

- The digital business models are highly integrated with multiple e-commerce operators being involved in the transaction chain.

- For instance, consider business models where there is one e-commerce operator (ACo) which merely lists the products of various other online sellers/ e-commerce operators (say BCo). In such case, where customer gets search results on ACo's platform and wants to buy a particular product, he will be redirected to BCo's platform. The customer can buy the product only on BCo's platform.
- In such case, there is a concern whether both ACo and BCo will be liable to withhold tax under S. 194-O specially since this may create duplicated levy of TDS on the same transaction. It also creates misperception on person who is actually liable to deduct TDS.
- Another example is where the NR e-commerce operator is operating on an onshore model i.e. through its Indian entity. In such case, if one argues that NR as well as Indian entity qualify as e-commerce operator, doubts arise whether both NR as well as Indian entity will be required to withhold taxes on the amount paid by Indian customers.

Recommendations

- It is recommended that CBDT Guidelines should clarify that the e-commerce operator which enters into contract for sale or service with e-commerce participant (supplier of the product or service) and has privity with the e-commerce participant for such transaction shall only be covered u/s. 194-O. The payments between the e- commerce operators including any convenience fee or internet processing fee or such other fees, should be excluded from the coverage of section 194-O. Similar provisions are also present under GST law which requires e-commerce operator to collect TCS

5. Exclusion of payment aggregator or payment gateways (covered under RBI Guidelines 2020 dated 17 March 2020) from S.194-O:

Amendment by FA 2020

- Section 194-O requires an e-commerce operator to withhold taxes on transaction of sale or service that is facilitated by such e-commerce operator.

Issue

- The broad scope of S. 194-O may also cover payment aggregators or payment gateways which act as intermediary by facilitating collection and settlement of payments between customers and e-commerce participants. The RBI Guidelines also require that the payment function should be undertaken through a separate entity as against the marketplace function. This will further reduce the visibility of payment systems over the transaction. The payment entities merely

assist in completion of payment arm of the transaction and are not involved in selling of goods or services.

Recommendation

- It is recommended that the CBDT Guideline should specifically clarify that the payment aggregators and payment gateways which are governed by RBI Guidelines are not covered under section 194-O.

6. Clarify the "digital or electronic platform or facility" does not cover e-mails, telephones:

Amendment in FA 2020:

- Explanation (c) to S. 194-O defines "e-commerce participant" as a person resident in India selling goods or providing services or both, including digital products, through digital or electronic facility or platform for electronic commerce. Further, "electronic commerce" is also defined as supply of goods or services or both, including digital products, over digital or electronic network.

Issue:

- It may be noted that orders for goods or services is booked not only through online portal of e-commerce operator but can also be procured by the customer by calling over telephone/ writing emails.

Recommendation:

- It may be clarified that S. 194-O would not apply to sale or service through e-mails or telephone do not fall into scope of "digital or electronic platform or facility"

B. Section 194-O: Coverage of e-commerce participant, definition of 'Service' and deminimis threshold limits

1. Extend de-minimis exemption to INR 10 lakhs and provide de-minimis exemption to all "e- commerce participants" under section 194-O Amendment by FA 2020:

S. 194-O(2) provides for a de-minimis exemption of INR 5 lakhs in case of certain ecommerce participants being individuals or HUF who furnish PAN/ Aadhaar to e- commerce operator.

Issue

- Benefit is not provided to small partnerships or companies which are upcoming and barely able to manage working capital. The proposed provision will hamper the growth of MSME the most and will discourage such small businesses from using e-commerce platform for expanding their business.

- The threshold limit of INR 5 Lakhs is very low on account of the fact that the income element in the consideration of Rs. 5 lakhs will be very low.
- Further, there is ambiguity whether once the payment exceeds the threshold limit, TDS is required only on the payment in excess of threshold or even on the amounts paid earlier below the threshold limit.

Recommendations

- Hence it is recommended that, the de-minims limit may be increased to at least INR 10 Lakhs or more.
- Further, it is recommended that the de-minims exemption of INR 10 lakhs be extended to all types of small e-commerce participants who furnish PAN or Aadhaar and not restricting to individuals and HUFs.
- Also, it may be clarified that once the payment exceeds the specified threshold, TDS is required only on the payment in excess of threshold limit.

2. Clarify that only services in the nature of 'Fees for Technical services' and 'Fees for Professional services' as defined under section 194J would attract TDS:

Amendment by FA 2020

- Section 194-O envisages payment of TDS by E-commerce companies for facilitating sale of goods and services of e-commerce participant through its digital electronic facility or platform. The term "services" includes 'fees for technical services' and fees for 'professional services', as defined in the Explanation to section 194J.

Issue

- There are doubts whether an Ecommerce company is required to withhold TDS only in case where the Ecommerce participants are rendering services in the nature of 'technical and professional services' as covered by the scope of section 194J, or other services would also attract TDS. In the absence of a clear mandate it may create commercial disputes between Ecommerce Companies and Ecommerce participants.

Recommendation

- An appropriate clarification should be issued to explain the scope of definition of 'services' for the purposes of section 194-O and to clarify that only services in the nature of 'Fees for Technical services' and 'Fees for Professional services' as defined in the Explanation to Section 194J would attract TDS under the Section 194-O.

3. Provide exemption from TDS obligation where there is sale of goods or supply of services by registered charitable trusts or institutions through e-commerce:

Amendment by FA 2020

- The Explanation to S.194-O defines e-commerce participant as a resident "person" selling goods or providing services through digital or electronic platform for electronic commerce. Accordingly, the such definition of e-commerce participant covers all persons being individual, HUF, companies, charitable trusts, institutions, etc.
- Further, the de-minims limit of INR 5 lacs under S. 194-O(2) is also provided only to such e-commerce participant who have status of individual and HUF.

Issue

- Due to wide scope of definition of e-commerce participant, charitable trusts and institutions, registered under S.11/12A and selling their goods through e-commerce platforms are also covered in the net of TDS.
- Such registered charitable trusts or institutions enjoy exemption under provisions of the Act for the charitable activity conducted by them. Hence, withholding taxes under section 194- O on gross amount of sales of such registered charitable trusts results in blockage of funds.
- Such entities shall not be able to utilise the said funds towards the charitable purpose. Furthermore, such entities shall be required to employ resources towards obtaining lower/nil deduction certification for section 194-O of the Act.
- The threshold of INR 5 lakhs provided under section 194-O(2) is also limited to individuals and HUFs and is not available to charitable trusts or institutions selling goods or services through e-commerce operator.

Recommendation

- In order to assist the legislative intent of promoting charitable activities in the society, it is recommended that if charities eligible for exemption under section 11/12AA are selling goods or providing services through e-commerce operators, then the ecommerce operator should be exempted from deducting tax on amount payable to such charitable entities. The charitable entities can furnish of declaration along with their PAN which e-commerce operator may report in quarterly TDS statement.

4. Allow for e-commerce operator to deduct taxes basis residential status declaration obtained from e-commerce participants at beginning of the year itself

Issue

- The definition of "e-commerce participant" indicates that the provisions of TDS under section 194-O are applicable to "resident" e-commerce participant.
- However, determining residential status is an extremely fact sensitive exercise. For instance, the residential status of an individual generally depends on the number of days of stay in India as per the parameters of S.6(1)/(1A) while in case of firm, AOP; the place

  of control and management is to be examined for determining residential status. Further, in case of companies, a resident entity can also be a foreign company having place of effective management (POEM) in India. An e-commerce operator is not possessed of sufficient details to determine such residential status of e- commerce participant. It creates additional compliance burden on the e-commerce operator to determine the tax residency of the e-commerce participant.
- Additionally, there is no clarity on which year's tax residency of e-commerce participant is to be considered by e-commerce operator while complying with Section 194-O of the Act. If the residential status of the e-commerce participant is to be examined for the tax year in which TDS under section 194-O of the Act is to be complied with, then parties may not even have sufficient information to determine residential status since residential status is generally concluded at the end of the tax year after considering the period of stay or location of management.
- Further, if the e-commerce operator delays its withholding obligation till end of the year when the residential status of e-commerce participant can be determined, then it shall result in non-compliance with TDS provisions of S.194-O which shall attract adverse consequences under provisions of ITA for the e-commerce operator.
- While this issue is not unique to TDS u/s. 194-O, but it is likely to create more difficulties in e-commerce transactions since s.194-O also covers normal sale of goods or commercial services like hotel bookings or flight bookings which are generally not liable for TDS.

Recommendation

- In order to avoid unintended hardship to e-commerce operator and ensure ease of compliance, it should be clarified that the e-commerce

operator can undertake TDS under section 194-O on the basis of residential status declaration obtained from ecommerce participants at the beginning of the year. Thereafter, the e-commerce operator should not be required to undertake any independent verification and should not be held liable for incorrect or false declaration (if any) given by e-commerce participant.

5. Where e-commerce operator withholds tax on gross amount of sale including his own commission, it may be clarified that e-commerce participant is not required to deduct TDS under section 194-H or any other TDS provision on commission paid to e-commerce operator

Amendment by FA 2020

- S.194-O(3) states that no tax is to be withheld under other provisions of Chapter XVII-B on transactions where the e-commerce operator has deducted tax at source u/s.194O(1) or where the e-commerce participant is excluded from the TDS provision by virtue of threshold limit of Rs.5 lakhs under S.194-O(2) of the Act.
- However, the proviso to S.194-O(3) states the above-mentioned relaxation is not applicable to amount received or receivable by e-commerce operator for hosting advertisement or in respect of services not connected with sale of goods or supply of services.

Issue

- In marketplace models, the operator could earn his income either as a convenience fee from the customer or as a fulfilment or commission fee from the seller or a combination of both. An ambiguity does arise on whether the phrase 'gross amount' would mean to include the fee charged by the operator
- Consider a scenario where e-commerce operator receives Rs. 100 out of which he retains Rs. 20 as his own commission and Rs. 80 is paid to e-commerce participant and the e-commerce operator has withheld taxes on entire Rs. 100.
- In such case, doubts arise whether the e-commerce participant is also obligated to withhold on e-commerce operator’s commission amount of 20 by virtue of the proviso to S. 194-O(3) or whether e-commerce participant can claim benefit of S. 194- O(3) which states no tax is to be withheld under other provisions of Chapter XVII-B on transactions where the e-commerce operator has deducted tax at source u/s.194-O(1)
- Since e-commerce operator deducts his own commission and pays net amount to e- commerce participant but deducts tax on gross amount of consideration, it is necessary to clarify that e-commerce

participant is not required to deduct tax on the commission amount. Otherwise it will add to the administrative burden of e- commerce participant to collect TDS amount from e-commerce operator and pay to the Government.

- Where e-commerce operator has withheld tax on gross amount of sale, it should be clarified that e-commerce participant is not required to deduct TDS on commission paid to e-commerce operator

6. Exports facilitated by the Indian e-commerce operator should not attract TDS Issue

- Given this vision of the Government to promote exports, TDS under section 194-O will add to the working capital burden of the e-commerce participant and thereby reducing his competitive advantage vis-à-vis other countries. This would only negatively impact the growth of the export sector for India.

Recommendation:

- It may be clarified that provision of section 194-O will not apply when the e-commerce operator facilitates sale of goods or services by a resident seller to a customer outside India i.e. only sales to customers in India are covered under the provisions.

C. Section 194-O: Issues on base amount for applying TDS under section 194-O

1. Clarify that amount liable for TDS under S. 194-O is net amount of sales and not gross sales receipts

Amendment by FA 2020

- Section 194-O(1) of the Act provides that the e-commerce operator shall be required to deduct tax at source on credit or payment made to e-commerce participants. The tax is to be withheld on "gross amount of such sales or services or both".

Issue

- In marketplace models and e-commerce industry, the "gross" amount of sale price of goods or services is not always recovered from the customer. It is common for marketplace to provide features of discount, guaranteed returns etc. The actual sale price after allowing discount is significantly lower than the gross value of sale of goods or services. Further, there is usually a 15 day window period for the buyers to return goods purchased through its platform. In such case, use of the term "gross" may result in difficulty for undertaking TDS compliance as the e- commerce operator becomes liable to pay tax on gross amount of sale price rather than the actual sale price.

- Even under GST law, TCS at the rate of 1% is collected by e-commerce operator on net taxable value of supplies which excludes sales return.

Recommendation

- In order to avoid ambiguity and cascading effect, it is recommended that the CBDT Guidelines should explicitly clarify that the gross amount of sale of goods or services for S.194-O should be computed after deducting discounts, sales return etc.

2. Clarify that TDS is not to be withheld on the GST/ indirect tax portion Amendment by FA 2020:

- S.194-O(1) provides that the e-commerce operator shall be required to deduct tax at source on credit or payment made to e-commerce participants. The tax is to be withheld on "gross amount of such sales or services or both".

Issue

- Further, under GST provisions, e-commerce operators charge and collect GST along with base sale price of goods or services. The use "gross amount" implies that the e- commerce operator is required to collect TDS even on the value of GST charged on goods or services.
- However, the CBDT has time and again clarified vide various circulars that TDS is not required to be deducted on service tax or GST component where the agreement/ contract or invoice specifies the amount of indirect taxes separately.

Recommendation

- Similar to clarifications issued under other TDS provisions, it should be clarified that ecommerce operator is not required to withhold tax on the amount of GST/ indirect tax that is collected from the customer.

3. Exclude shares, securities, prepaid instruments like wallets or gift cards which are money or equivalent of money, money, etc. from the scope of "goods" and "services"

Amendment by FA 2020

- The definition of electronic commerce under clause (a) of Explanation to S.194-O is provided to mean supply of goods or services or both, including digital products, over digital or electronic network.

Issue

- The definition of "electronic commerce", "e-commerce operator" under S. 194-O seems wide enough to cover conventional and well-regulated platforms/ markets such as stock exchange or power exchange. Considering the intent of S. 194-O is to tax e-commerce

transactions and tax evaders, if any; it may not be correct to levy such obligation on stock exchange or power exchange which are conventional and well-regulated sectors.

- Further, there is ambiguity on whether sale of prepaid instruments like gift cards or assignment of loans by financial institutions or discounting of debts or rent receivables are covered within the scope of section 194-O of the Act.

Recommendation

- It is recommended to introduce suitable clarification in the CBDT Guidelines to exclude certain terms like shares, securities, power units, money, all form of prepaid instruments from scope of "goods" under provisions of Section 194-O.

D. Section 194-O: Issues on consequential exemption from other TDS provisions

1. Clarify that customer is relieved from withholding tax under other provisions of Chapter-XVIIB once e-commerce operator has deducted tax under section 194-O

Amendment by FA 2020

- S.194-O requires the e-commerce operator to deduct tax at source on transactions where sale of goods or provision of services of e-commerce participant takes place through the digital or electronic platform of the e-commerce operator. S.194-O applies even if direct privity exists between buyer and seller.
- S.194-O(3) states that no tax is to be withheld under other provisions of Chapter XVII- B on transactions where the e-commerce operator has deducted tax at source u/s.194O(1)

Issue

- Prior to introduction of S. 194-O, the customer was obligated to withhold taxes under Chapter XVII-B (e.g. S.194C, S.194J) when such customer avails goods or services from an e-commerce participant (even where such goods or services are rendered through the digital platform of e-commerce operator). Since there is direct privity between customer and e-commerce participant, the customer becomes liable to deduct tax at source.
- However, post 194-O, where the aforesaid transaction is undertaken through the digital platform of the e-commerce operator, such e-commerce operator is obligated to withhold taxes on amount of sale or service facilitated through its platform
- While S. 194-O(3) states no tax is to be withheld under other provisions of Chapter XVIIB on transactions where the e-commerce

operator has deducted tax at source u/s.194O(1), to allay any doubts or apprehensions on part of customers, it is necessary to clarify that the customers are relieved from withholding under other TDS provisions like

s.194C, s.194J, etc to avoid any duplicated TDS by customer and e-commerce operator on the same transaction.

- Further, the buyer may not be aware whether the e-commerce operator will deduct TDS under section 194-O and not deduct due to de-minimis threshold under section 194O(2).

Recommendation

- It is recommended that even if services provided by e-commerce participant are in the nature of those covered by existing TDS provisions like s.194C or s.194J or s.194H or s.194I, etc, it may be clarified that TDS u/s. 194-O shall override all such TDS provisions relieving the customer from TDS obligation and TDS obligation will be on e-commerce operator under section 194-O.

Section 206C (1G)

A. Scope of definition of 'Overseas tour program package'

1. Clarify that collection of TCS will not be applicable in case of standalone booking for air ticket or hotel accommodation or ancillary activities related to foreign tours in isolation:

Amendment by FA 2020

- Section 206C, sub-section 1G, clause (b), seller of an overseas tour program package, who receives any amount from a buyer, being the person who purchases such package, shall, collect TCS from the buyer.
- Further, as per Explanation to section the term "overseas tour program package" has been defined to mean any tour package which offers visit to a country or countries or territory or territories outside India and includes expenses for travel or hotel stay or boarding or lodging or any other expenditure of similar nature or in relation thereto.

Issue

- Keeping in with the above definition of overseas tour package, we understand that the TCS shall be applicable on payments made for booking of bundled overseas tour package as it offers visit to foreign country and includes expenses for hotel stay, sightseeing, etc. However, a standalone international hotel booking or merely booking

an entry ticket for an event outside India cannot be treated as an offer to travel outside India.

Recommendation

- An appropriate clarification must be issued to clarify that collection of TCS will not be applicable in case of standalone booking for air ticket or hotel accommodation or ancillary activities related to foreign tours in isolation.

2. Section 206C (1G): Non-resident buyers should be excluded from the applicability of TCS provisions

Amendment by FA 2020

- As per section 206C, sub-section 1G, clause (b), buyer means a person who purchases overseas tour package. This would include non-resident buyers as well.

Issue

- A non-resident can also buy such tour packages from an India travel agents. Application of TCS provision on non-resident could not be the objective of the Government.
- Especially where non-residents are not required to have PAN, double rate of TCS will cause undue hardship for Non-resident buyers and raise the cost of package for them. This may also lead to loss of revenue as these buyers can also book such services from foreign travel agents.

Recommendation

- It is recommended that the non-resident buyers should be excluded from the applicability of TCS provisions.

Summary of the Recommendations in respect of Section 206C(IG) and Section 194-O of the Act

(a) Section 194-O: Coverage of e-commerce operator:

(i) Exclusion of such platforms from scope of e-commerce operator which merely provide list and information of products but does not enable sale of such products.

(ii) E-commerce operator be liable for TDS under section 194-O only when payment is routed through such e-commerce operator.

(iii) Clarify that section 194-O of the Act does not apply in scenarios where e-commerce operator is selling own goods on its own platform.

(iv) Considering the definition of “e-commerce operator” under GST laws and S. 194-O is the same, ITA may consider applying S. 194-O only to such players who are registered “e-commerce operator” under GST laws.

(v) In certain cases, online sale transaction takes place through multiple e-commerce operators. Similar to GST provisions, it should be clarified that the e-commerce operator who enters into contract for sale or service with e-commerce participant and has privity with the e-commerce participant for such transaction shall only be covered under section 194-O.

(vi) Exclusion to be provided to payment aggregator or payment gateways (covered under RBI Guidelines 2020 dated 17 March 2020) which merely facilitate the payment leg of the sale transaction and function similar to a bank.

(vii) Clarify the “digital or electronic platform or facility” does not cover sales concluded through e-mails, telephones

(b) Section 194-O: Coverage of e-commerce participant, definition of ‘Service’ and deminimis threshold limits:

(viii) Extend de-minimis exemption to INR 10 lakhs and provide de-minimis exemption to all “e-commerce participants” u/s. 194-O and clarify that TDS will apply only on amount of payment which exceeds the threshold limit

(ix) Clarify that only services in the nature of ‘Fees for Technical services’ and ‘Fees for Professional services’ as defined in the Explanation to Section 194J would attract TDS under Section 194-O

(x) Provide exemption from TDS obligation where there is sale of goods or supply of services by registered charitable trusts or institutions through e-commerce

(xi) Allow for e-commerce operators to deduct taxes basis residential status declaration obtained from e-commerce participants at beginning of the year itself

(xii) Where e-commerce operator withholds tax on gross amount of sale including his own commission, it may be clarified that e-commerce participant is not required to deduct TDS u/s.194-H or any other TDS provision on commission paid to ecommerce operator

(xiii) Section 194-O should not apply when e-commerce operator facilitates sale of goods or services by a resident seller to a customer outside India (i.e. Exports)

(c) **Section 194-O: Issues on base amount for applying TDS under section 194-O**

(xiv) Tax should be withheld on amount of sale of goods net of sales returns, discounts, etc. rather than gross amount of sales.

(xv) Tax should be not be withheld on amount of GST/ indirect taxes which are collected from the customers.

(xvi) (xvi) Exclude shares, securities, prepaid instruments like wallets and gift cards, money, etc. from the scope of "goods" and "services"

(d) **Section 194-O: Issues on consequential exemption from other TDS provisions**:

(xvii) Clarify that customer is relieved from withholding tax under other provisions of Chapter-XVIIB once e-commerce operator has deducted tax under section 194-O

(e) **Section 206C (1G): Scope of definition of 'Overseas tour program package'**:

(xviii) Clarify that collection of TCS will not be applicable in case of standalone booking for air ticket or hotel accommodation or ancillary activities related to foreign tours in isolation

(f) **Section 206C (1G): Exemption to Non-resident buyers**:

(xix) Non-resident buyers should be excluded from the applicability of TCS provisions.

Section IV

Suggestions for Atmanirbhar Bharat - Encourage Expenditure on Scientific Research and Innovation

4.1 Encourage Expenditure on Scientific Research

It is well recognised that scientific research is the lifeline of business in all countries of the world. Withdrawal of weighted deduction in respect of scientific research expenditure will put a dent to the 'Make in India' initiative of the Government.

Innovation and digitisation is not limited to industrial sectors and has gained momentum in service sectors as well.

Section 35(2AB) of the Act extends weighted deduction towards the expenditure incurred towards scientific research on in-house research and development facility as approved by the prescribed authority to companies engaged in the business of

- bio-technology; or
- manufacture or production of any article or thing (other than those specifically excluded for purposes of this tax incentive).

The Finance Act, 2016, with a view to phase out weighted deduction under section 35(2AB) of the Act, restricted the allowability of expenditure incurred on scientific research (other than expenditure in the nature of cost of any land or building) on in-house research and development facility to 150% from 200% with effect from April 1, 2017 to March 31, 2020 and to 100% from previous year 2020-21 onwards.

Withdrawal of weighted deduction in respect of scientific research expenditure is detrimental to the 'Make in India' initiative of the Government.

Issues related to deduction under section 35(2AB)

- There is ambiguity with regard to claim of weighted deduction in respect of expenditure on outsourced research and development activities, foreign patent filing expenditure, clinical trial activities carried outside the approved facilities, expenditure on any payments made to members of the board of directors or any other part time employees engaged in research and development etc.

  The Hon'ble High Court of Gujarat in the case of Cadila Healthcare Limited [2013] 31 taxmann.com 300 (Gujarat) has also confirmed that clinical trials conducted outside the approved in-house research and development laboratory is eligible for deduction under section 35(2AB) of the Act.

- Indian innovators filing patent applications in foreign countries are required to do so under The Patents Act, 1970. Furthermore, Indian companies incur substantial costs in defending their patent rights and applications in and outside India.

  Currently, as per DSIR guidelines amount spent by a recognized in-house R&D towards foreign consultancy, building maintenance, foreign patent filing, interest on loan for the

R&D facility etc. are not eligible for weighted deduction under Section 35(2AB) of the Act. Such expenses are essential in carrying out research at the approved R&D centres. It is suggested that DSIR guidelines should not deal with the allowability or disallowability of any expenditure incurred on in-house R&D facility. It is further suggested that the specific clarity be provided regarding allowability of deduction under section 35(2AB) of the Act in respect of the aforesaid expenditure and DSIR guidelines be suitable aligned with the provisions of the Act to avoid any litigation on this matter.

- Further, specifically in the pharma sector, pharmaceutical discovery is a lengthy, risky and expensive proposition. In this business environment, necessitated by the current business needs, sometimes companies incur expenses towards scientific research outside their R&D facility.

  Accordingly, expenditure incurred outside the approved R&D facility by pharma companies' i.e. towards clinical trials (including those carried out in approved hospitals and institutions by non-manufacturing firms), bioequivalence studies conducted in overseas CROs and regulatory and patent approvals, overseas trials, preparations of dossiers, consulting/ legal fees for filings in USA for new chemicals entities (NCE) and abbreviated new drug applications (ANDA) which are directly related to the R&D, etc. be specifically clarified to be falling under the ambit of section 35(2AB) of the Act.

- India is globally recognized as an attractive jurisdiction for outsourcing owing to its affordable, skilled and English-speaking manpower. Outsourced R&D work is becoming a key area of growth for the Indian services sector however there are no specific tax benefits available to units engaged in the business of R&D or contract manufacturing.

- Currently, there seems to be an ambiguity with respect to whether a company engaged in the business of development and sale of software or providing IT services or ITES is eligible for weighted deduction on the R&D expenditure incurred by it.

- 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 under section 35(2AB) of the Act.

- Approval under section 35(2AB) of the Act is available only after completion of the research and development facility and therefore, the expenditure incurred prior to approval which normally involve substantial expenditure, does not get the benefit of weighted deduction.

- Eleventh Schedule contains articles/things like cosmetics, toilet preparations, toothpaste, dental cream, tooth powder, soap, photographic apparatus, office machines, steel furniture, safes, etc. There is no logical reason why research expenditure on the abovementioned articles should not be allowed.

- Total Income for the purpose of section 115BAA and 115BAB of the Act has to be computed without claiming deduction under section 35(2AB) of the Act. Scientific

research is the lifeline of business in all countries of the world and must be encouraged by way of continuation of deduction for expenditure on scientific research.

Recommendations

- It is recommended that weighted deductions allowed under the Act to various modes of scientific research expenditure be continued. The Government can also consider introducing benefits in the form of research tax credits which can be used to offset future tax liability (similar to those given in developed economies).
- It is suggested that weighted deduction @ 200% under section 35(2AB) of the Act be restored to promote research and development in the manufacturing space and to make India a manufacturing hub.
- It is further suggested that it may be specifically clarified that scientific research shall also include research activities in service sector.
- It should be suitably clarified that the expenditure on patent filing in and outside India is eligible for deduction under section 35(2AB) of the Act.
- It is suggested to extend tax benefits to units engaged in the business of R&D or contract manufacturing to provide impetus to R&D in India.
- Presently, there are no specific provisions which enable carry forward of R&D benefits separately. Considering the time taken in R&D activity, and its benefit available after a very long gap, it is suggested that it should be clarified that the unutilized R&D deduction should be available for carry forward and set off indefinitely (as in the case of unabsorbed depreciation).
- It is further suggested that the existing provisions of the Act should specifically allow weighted deduction in respect of expenses incurred outside the R&D facility which are sometimes necessitated by the industry's business needs. Additionally, it should be clarified that where the risk of doing research is assumed by a company, the entire cost of R&D activities (whether outsourced or undertaken in-house) is eligible for weighted deduction in the hands of company undertaking the risk.
- Provide weighted deduction for expenditure incurred on internally developed intangible assets under Section 35(2AB) of the Act.
- Suitable amendment be made in section 35(2AB) of the Act to provide that once the approval is granted under section 35(2AB) of the Act the same should be made effective from the date of initiation of the said research and development facility and accordingly, the entire expenditure incurred on establishment of such facility would be eligible for deduction under section 35(2AB) of the Act.
- It is recommended that deduction for expenditure on scientific research as prescribed under section 35(2AB) of the Act should be continued for companies opting to pay tax at concessional rate as per section 115BAA and 115BAB of the Act.

4.2 Dilution of Tax Incentive under Section 35AD by insertion of Section 73A of the Act

Issue

- The underlying idea behind allowing the investment linked incentive granted under Section 35AD of the Act is to enable the taxpayer to set-off the business losses incurred by this write-off against the taxable profits from their existing businesses and reduce their tax liability in the year of deduction and thereby to provide part of the resources of investment required for setting up of the businesses. The investment linked tax holiday under section 35AD is considered to be a mode of 'balance sheet financing'. However, the incentive so intended cannot be achieved owing to Section 73A of the Act, which restricts the set-off/carry forward of losses by specified business only against the profits and gains, if any, of any other specified business carried on by the taxpayer in that AY and the amount of loss not so set-off can only be carried forward and set-off against profits from specified business in the subsequent AYs.

Recommendation

- The losses from the specified business under Section 35AD of the Act ought to be made eligible for set-off against profits from other businesses of the taxpayer, and not restricted to be set-off against only the specified businesses, as it is not always the case that the taxpayer would only be carrying on the 'specified business'. In light of the above, section 73A of the Act should therefore be deleted.

Clarification on Amendment to Section 35AD(3) of the Act

Issues

- Section 35AD(3) of the Act prevents a taxpayer from claiming dual deduction in respect of the same business.
- It appears that if a taxpayer carrying on a specified business does not claim deduction under section 35AD, he may opt for deduction under the relevant provisions of Chapter VI-A or Section 10AA, if the same exist for such business and it is more beneficial.

Recommendations

- A clarification should be issued that the taxpayer may exercise an option (where available to the taxpayer) to avail tax incentive under section 35AD or Chapter VI-A/ Section 10AA of the Act, depending upon which is more beneficial to the taxpayer.
- Further, it is suggested that a clarification may also be issued that in the event the taxpayer opts for the investment linked incentive under Section 35AD of the Act and the same is denied/rejected at time of assessment proceedings (could be on account of nonsatisfaction of prescribed conditions), in such case the taxpayer is eligible to make an alternative claim under Chapter VI-A or Section 10AA, on satisfaction of the conditions provided therein, notwithstanding the requirement stipulated in Section 80A (5) of the Act or 10AA of the Act. This is because, a taxpayer who is otherwise entitled to deduction in respect of qualifying profits of the specified business would lose such deduction on account of Section 80A(5) of the Act that mandates a claim for deduction

under chapter VI-A be made in its return of income. As the taxpayer would not have claimed deduction under provisions of Chapter VI-A/ Section 10AA of the Act in its return of income since claim was made under Section 35AD of the Act, such taxpayer would be precluded from claiming deduction in view of Section 80-A(5)/ Section 10AA of the Act.

Prescribe separate audit report form or modify Form 10CCB to include details of investment linked deduction under section 35AD

- It is recommended that specific Form should be prescribed for filing audit report as required by section 35AD(7) of the Act since Form 10CCB (presently applicable only for profit linked deduction under section 80I(7), 80IA(7), 80IB, 80IC) does not specifically capture investment linked deduction under section 35AD of the Act. Alternatively, Form 10CCB may be modified to include details relating to investment linked deduction under section 35AD of the Act. Further, such form may also require the taxpayer to specify whether or not it wants to avail deduction under section 35AD of the Act for the relevant previous year.

4.3 Patent Box Regime – Section 115BBF

The Finance Act, 2016 introduced a new provision under which income earned by a qualifying taxpayer from the exploitation of a patent would be taxed at a preferential rate of 10%. No deduction of any expenditure or allowance would be allowed in computing the income under this regime, and the income qualifying for the preferential rate should be by way of royalty in respect of a patent developed in India. 'Eligible taxpayer' has been defined to mean a person resident in India, who is the true and first inventor of the invention and whose name is entered on the patent register as the patentee in accordance with Patents Act, 1970.

(a) True and First Inventor

Issues

- The benefit of provision is restricted to 'true and first inventor of the invention'. Even a person who is jointly registered with 'true and first inventor' should be treated as 'true and first inventor'.
- In view of following features under the Patent law, the benefit of the provision may be denied to firms/LLPs/companies who register the patents jointly with 'true and first inventor' who may be an employee even though they may have incurred significant expenditure for development of the patent and they are first economic owners of such patent.
- Under the Patents Act, following persons can apply for patent (a) a person claiming to be true and first inventor of the invention (b) an assignee of the true and first inventor in respect of right to make an application and (c) legal representative of a deceased person who immediately before his death was entitled to apply.

- It is also settled under the Patent Act that a company or firm cannot claim to be 'true and first inventor'. They can only apply as assignee of true and first inventor.

Recommendation

- It is, hence, recommended that the condition of joint patentee also being 'true and first inventor' be omitted. If the intent is to allow benefit only to first person to register patent, the phrase 'being the true and first inventor of the invention' used in context of joint person may be substituted with the phrase 'being the assignee of the true and first inventor in respect of the right to make an application for a patent'.

(b) Patent Registered in India as also in a Foreign Country

Issues

- The requirement of patent being registered in India under the Patents Act raises an ambiguity whether royalty received from overseas in respect of patent which is registered both in India and outside India will be denied the benefit on the ground that the royalty is relatable to foreign patent and not Indian patent.
- It may be noted that Patent law is territorial in nature and the exclusive rights cannot be exercised in any country unless the patent is registered in that country as per local patent law.
- The condition of patent being developed in India ensures that the benefit of PBR is restricted to inventions which are developed in India. Benefit should not be denied for royalty received from overseas countries for the same invention by registering it outside India.

Recommendation

- It should be clarified that royalty received from overseas for a patent which is registered in India as also in a foreign country also qualifies for concessional rate of tax. The benefit should not be denied on the ground that such royalty is attributable to foreign patent.

(c) Benefit of Patent Regime be allowed to Successor

Issue

- There is no provision in section 115BBF of the Act for continuation of the concessional rate of tax to the successor in case of tax neutral mergers and demergers and/or succession by way of slump sale or death of the inventor which may result in unwarranted denial of benefit and impediment to ease of doing business.

Recommendation

- In case of a business re-organisation in the form of merger, demerger etc., the successor entity and in case of death of the patent owner, its legal heir/inheritor of the patent should be considered as eligible to claim the benefit provided such successor/legal heir satisfies the condition of being a resident of India.

(d) Extend benefit to Royalty Income in respect of Patents applied but Registration awaited

Issues

- Royalty from a patent which is 'registered' alone qualifies for the patent box regime. If royalty income is earned when patent application is filed but registration is awaited, there may be unwarranted denial of the benefit.
- Under the current process of Patent Law, it takes minimum of 5 to 6 years for a patent to be registered but the registration relates back to the date of filing application. But it is possible for the inventor to license out the invention and start earning royalty from the date of application.
- If benefit is denied on the ground that patent is applied but not registered, there is no back up provision to grant the benefit for earlier years when the patent is finally registered.

Recommendations

- Hence, it is recommended that the concessional tax regime be extended to royalty income earned from patents which are applied for and awaiting registration as well.
- Alternatively, amendment may be made in the Act to provide that assessments for the period of royalty earned between the date of application to the date of registration shall be rectified to grant the benefit without any time limit once patent is registered.

(e) Extend benefit to Capital Gains arising in the hands of the Taxpayer Issues

- The concessional tax rate is not applicable in respect of royalty received as capital gains. The taxpayer may exploit the patent by outright transfer which has no differential impact merely because for one assessee the amount is assessable as business income whereas for other it is assessable as capital gains income. There is no reason to exclude amount which is chargeable as capital gains in the hands of the taxpayer.

Recommendations

- It is recommended that concessional regime should also be extended to capital gains arising in the hands of the taxpayer on account of patent.

(f) Extend Benefit to other Intellectual Property Rights

Issue

- Section 115BBF of the Act provides the benefit of reduced rate of tax to only royalty income derived from patents subject to specified conditions. This may partly achieve the intended objective of the government behind introduction of this provision i.e. to encourage indigenous research & development activities and to make India a global R & D hub.

Recommendation

- The current income tax law treats other intellectual rights like any know-how, copyright, trade-mark, license, franchise or any other business or commercial right of similar nature in the same vein as patent. Hence, there appears to be no reason not to extend the benefit of section 115BBF to income from other intellectual property rights.
- It is recommended that the benefit of concessional rate of tax of 10% of income by way of royalty in respect of a patent developed and registered in India be also extended to other intellectual property rights like know-how, copyright, trademark etc.

(g) Extend the Benefit from Self-exploitation of Patents by Manufacture and Sale of Articles

Issue

- Section 115BBF of the Act provides the benefit of reduced rate of tax to only 'royalty' income derived from patents. This suggests that companies which hold patents and exploit them commercially by manufacturing and selling goods / articles may not qualify for the PBR, since they do not earn 'royalty' income per se. This will necessitate division of businesses into patent holding companies and companies that exploit the patent, which is artificial and serves no commercial purpose.

Recommendation

- It is recommended that a concessional rate be extended to companies that exploit their own patents in the manufacture and sale of articles, by imputing a 'royalty' income determined on the basis of the arm's length principle.

Section V

Provisions in relation to Start-ups

5.1 Pertinent issues in relation to start-up

Issues

Withdrawal of exemption under section 56(2)(viib) upon non-compliance by start-ups with any of the conditions laid down in DPIIT Notification dated 19 February 2019

- As per DPIIT Notification, the start-up is required to satisfy various conditions in order to avail the exemption to section 56(2)(viib) of the Act.
- The conditions to be satisfied at the time of issuance of shares and for availing exemption under section 56(2)(viib) are divided into (i) recognition conditions and (ii) threshold conditions.
- The Notification also provides for satisfaction of certain end use conditions for the purposes of claiming/retaining the exemption.
- The second proviso to section 56(2)(viib) of the Act provides for withdrawal of exemption if 'any' of the conditions specified under the DPIIT Notification No. G.S.R. 127(E) dated 19 February 2019 is not fulfilled.
- Thus, as per plain reading of the proviso, the claw back provisions are attracted even upon the non-fulfillment of recognition or threshold condition in subsequent years by the start-ups i.e. post the issue of shares. For example, if the aggregate of share capital and share premium exceeds Rs. 25 Cr in any of the years subsequent to the issuance of shares, it could result in withdrawal of the exemption.
- However, the DPIIT Notification suggests that only when end use conditions are not satisfied (after the issue of shares), the exemption shall be withdrawn retrospectively.
- Thus, the second proviso to section 56(2)(viib) of the Act may be amended to provide explicitly that the exemption shall be retrospectively withdrawn only if the start-up fails to comply with the "end-use condition(s)" in DPIIT/DIPP Notifications which the start-up is expected or mandated to comply in subsequent years post issuance of shares.
- In other words, the claw back provisions under the Act should not apply if there is breach of recognition or threshold condition by the start-up in subsequent years.

Granting relaxations from inquiry under section 68 to Cat-II AIF investors and genuine investments received by start-ups

- Finance Act 2012 amended section 68 of the Act to require unlisted companies to explain 'source of source' in respect of share application/ capital/premium, etc. and also introduced section 56(2)(viib) of the Act to tax excessive premium received by unlisted companies from residents. But in both provisions, exception was carved out for share capital raised from VCF/VCC.

- Finance (No.2) Act 2019 has amended section 56(2)(viib) of the Act to extend the carve out to all the Category I and Category II SEBI registered AIFs. However, similar consequential amendment is not made to second proviso to section 68 of the Act. Since Category I and II AIFs are regulated entities like VCC/VCF, they should be carved out from second proviso to section 68 of the Act as well.

Other recommendations for amendment in DPIIT Notification of 2019

- Issue of shares to Cat I (except VCC/ VCF) and Cat-II AIF investors, which are exempt, should be excluded from calculation of threshold of aggregate share capital and premium of Rs. 25 Crs in case of start-ups
- Accordingly, suitable amendment may be incorporated in DPIIT Notification dated 19 February 2019.

5.2 Extend deferral of taxation on ESOP perquisite to all employees - Amendments to Section 156(2), Section 191(2) and Section 192(1C) be modified to refer to an employer being a “start-up” which is recognised by DPIIT

The provisions of deferral of tax on ESOP perquisite are applicable in cases where the ESOP shares or sweat equity shares are allotted directly or indirectly by start-up which is eligible under section 80-IAC of the Act. Accordingly, the ESOP shares or sweat equity shares allotted by start-ups other than “eligible start-up” are not covered under the new scheme of deferral of tax on income.

Issue

- Employees of a start-up company, which is recognised by DPIIT but is not covered under section 80-IAC of the Act- say, because it is not incorporated between 1 April 2016 and 1 April 2021, may not be able to get the benefit of deferral of tax. The amendment will benefit employees of only 220 such ‘eligible start-ups’ leaving out employees of other approx. 28,000 start ups registered with DPIIT4.
- The Explanatory Memorandum to Finance Bill, 2020 states that the scheme for deferral of ESOP scheme is introduced for start-ups as payment of TDS or tax at the stage of exercise of option creates difficulty due to lack of adequate liquidity with the employer and employees. Further, the component of ESOP shares forms a larger part of salary income of employees of start-ups.

  It may be noted that the above circumstance of liquidity crunch may not be restricted to a case of start-up but may extend to other taxpayers as well. In fact, the cash flow issue which is sought to be relieved by the new provision is faced by all unlisted companies (particularly targets of investments by VC and PE investors).

Recommendation

- The amendment deferring the collection of tax on ESOPs exercised by employees of ‘eligible start ups’ (i.e. start-ups set up on or after 1 April 2016 approved by Inter

[4] Source: https://www.startupindia.gov.in/content/sih/en/startup-scheme.html

Ministerial Board for section 80IAC benefit) is welcome, since it partially addresses cash flow issue for employees and employer.

- It is recommended that the benefit of deferral of tax should be extended for ESOPs granted by all employers since cash flow problem is faced by all employees. Hence, it is suggested to extend the benefit to all the employees.

  Without prejudice, it is recommended that the benefit can be extended to all start-ups registered with DPIIT and should not be restricted to start-ups eligible under section 80IAC of the Act. Hence, it is recommended that the language of the amendments to Section 156(2), Section 191(2) and Section 192(1C) be modified to refer to an employer being a "start-up" which is recognised by DPIIT.

5.3 Provide clarity on taxation of deferred consideration under capital gains

Issues

(i) With the growth of the Indian economy and rapid globalisation, business restructuring has gained significant prominence in India with entities perennially on the look-out for funding and/or inorganic growth opportunities. Among others, one of the major drivers of decision making is the tax efficiency of such restructuring.

(ii) One of the common features of such new-age business reorganisations is to link the payment of consideration for transfer with the future growth prospects of the business i.e. the consideration is contingent upon certain parameters such as growth, profits, EBIDTA, etc. achieving their prescribed level.

(iii) This is especially true for the start-up sector where given the large valuations seen based on future potential, there is often a difference in value perception between the promoters and the potential investors.

(iv) However, the currently prevailing provisions of the Act do not have clarity on the taxation of such contingent consideration i.e. whether the tax implications would relate back to year of transfer or the same would be brought to tax in year of receipt. Even the judiciary seems to be divided on this issue with rulings for and against both views[5].

Recommendation

(i) In order to provide clarity, as well as to boost the Indian Start-up sector, appropriate provisions may be introduced to clarify that such capital gains taxation will arise only in the year in which contingent consideration becomes due as per terms of agreement.

(ii) This would also be in line with the rationale adopted for taxation of enhanced compensation on compulsory acquisition which is taxed in year of receipt [in S. 45(5)] or taxation of capital gains arising from conversion of capital asset into stock in trade which is taxed in year of sale of such stock [in S. 45(2)].

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[5] For instance, refer SC ruling in Ghanshyam (HUF) [315 ITR 1 (SC)] and Delhi HC in Ajay Guliya [TS-520-HC-2012 (Del)] which favoured contingent consideration relating back to year of transfer and hence being taxable in year of transfer. Also refer Bombay HC ruling in Mrs. Hemal R Shete (ITA No. 2348 of 2013) which favoured contingent consideration being taxable in year of determination of such contingent consideration

Section VI

Issues related to Significant Economic Presence, General Anti-Avoidance Rule, Place of Effective Management and Equalization Levy on online advertisement revenues

6.1 Issues related to Significant Economic Presence (SEP)

Background

- In order to address Base Erosion and Profit Shifting arising from the rapidly digitalising economy, Finance Act 2018 expanded the concept of business connection to include a new nexus rule based on SEP to tax the digital economy, which hitherto enabled entities world over to carry out business in India without an actual physical presence, and thereby escape taxation in India.

- As per SEP provisions, a Business Connection will be constituted in India based on below parameters:

  a) Revenue-linked condition: Any transaction in respect of any goods, services or property carried out by a Non-Resident with any person in India, including provision of download of data or software in India, if the aggregate of payments arising from such transaction or transactions during the tax year exceeds the amount as may be prescribed; or

  b) User-linked condition: Systematic and continuous soliciting of its business activities or engaging in interaction with such number of users in India as may be prescribed

- Further, once an SEP is triggered, only so much of income as is attributable to the transactions or activities referred to in (a) or (b) above shall be taxable in India.

- Additionally, income attributable to transactions and activities referred to in condition (a) and (b) shall also cover income from:

  - Such advertisement which targets a customer who resides in India or who accesses the advertisement through internet protocol (IP) address located in India;

  - Sale of data collected from a person who resides in India or who uses IP address located in India; and

  - Sale of goods or services using data collected from a person who resides in India or who uses IP address located in India

- In this regard, CBDT through Notification No. 41 dated 3 May 2021 prescribed revenue and user thresholds as below thereby putting SEP provisions into application.

  - For revenue-linked condition stated in (a) above, a revenue threshold of INR 2 crores (INR 20 million) shall be applicable;

  - For user-linked condition stated in (b) above, a user threshold of 3 lakhs (0.3 million) shall be applicable

- These thresholds are applicable from 1 April 2022 aligning with the effective date of the new nexus rule.

Modify the existing SEP provisions in light of global consensus solution reached under Pillar One discussions

Background and Issue:

- As stated above, provisions of SEP were introduced in the Act in 2018 (then subsequently modified vide Finance Act 2020) in lieu of ongoing global discussions under G20-OECD BEPS project on taxation of digitalised economy under BEPS Action 1.
- Subsequent to BEPS Action 1, the OECD continued its strive for a global consensus solution under two pillar approach wherein Pillar One particularly focused on "Tax Challenges Arising from Digitalisation". On 1 July 2021, the long awaited global consensus was reached and currently, more than 134 countries6 of BEPS inclusive framework (IF) have agreed on the key components of the Pillar One framework including, scope, nexus, allocation of profits under Amount A etc.
- The provisions of SEP are fairly different from agreement solution under Pillar One. The key difference being while SEP determines taxable nexus of NR at entity level qua the transactions/activities undertaken with person/ users in India, Pillar One proposes to establish nexus and attribution profits at Multinational enterprise (MNE) group level.
- Since SEP was introduced in light of BEPS discussions, it is our humble suggestion that provisions of SEP be tailored to fit them in line with global consensus solution. The Blueprint released by OECD in October 2020 also acknowledged that implementation of Pillar One proposals will require changes not only in treaty but also in domestic laws. The report states that BEPS IF members would need to create domestic taxing rights consistent with the design of Amount A, provide method for elimination of double taxation for residents, dispute prevention and resolution mechanisms, etc.

Recommendation:

In order to ensure consistency with Pillar One solution, we propose the following changes be made to SEP provisions:

- **Applicability of SEP to MNE groups with global turnover or gross receipts of above €750 million and having profitability of 10[7]%:** Similar to global consensus, a MNE level revenue threshold should be introduced in the Act. While the currently agreed revenue threshold of €20 billion (to be subsequently reduced to €10 billion after 7 years) may be fairly high, India may consider a threshold in line with CbCr provisions i.e. €750 million qua MNE group. It will ensure that the companies covered under CbCr are also covered under new SEP provisions under the Act. This will also ensure that domestic source rule taxation is wider than treaty threshold and entities of MNE group not having treaty protection will be covered under domestic taxation.

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[6] Data as on 31 Aug 2021

[7] Profit before tax/revenue

- **Exclusion for extractive industry and Regulated Financial services sectors:** Businesses engaged in extractive industry[8] and financial sector[9] such as banking, insurance, asset management etc. be excluded from scope of SEP in line with Pillar 1 scope exclusion
- **Establish taxable nexus in India basis revenue generated by MNE group:** Under Pillar One IF solution, an MNE group establishes nexus with a market jurisdiction only where such MNE earns revenues of more than € 1 million from such market (€ 250,000 from countries with GDP less than € 40 billion) . On similar lines, SEP provisions need to be amended where MNE earns revenues from Indian market above certain threshold. Since domestic taxation rules need to be wider, the threshold of € 250,000 may be considered for SEP. Thus, the user-based nexus rule under existing SEP rule should be deleted. The attribution based on targeted advertisement audience from India or data collection from India or sale of goods/services based on data collected from India should also be deleted.
- **Introduce profit attribution rules in line with Pillar One solution:** Under Pillar One proposal, a portion of MNE level profits are allocated to market jurisdiction basis a formulary approach. As per the formula agreed, 20-30% of MNE non routine profits[10] will be allocated to market jurisdictions with nexus using a revenue-based allocation key. Such formula agreed under global consensus needs to be introduced under the Act as well

Without prejudice to above, if the provisions of SEP are not amended in light of Pillar One discussions and/or pending implementation of Pillar One proposals, we humbly request to consider following representations on issues related to SEP

Exemption should be provided from procedural requirements (like obtaining PAN, filing return, etc.) where SEP is triggered but treaty protection is available

Issue

- While the SEP provisions have become operational as source rule, it may have no applicability to taxpayers who are from treaty jurisdictions. Such fact is also noted by the Explanatory Memorandum to Finance Bill 2018 which observed that *"unless*

[8] Extractive businesses are those engaged in the exploration for, and extraction from the earth's crust of, non-renewable natural resources such as hydrocarbons and minerals, the processing and refining of those resources into usable commodities, and the sale of those commodities. As per the OECDs "Tax Challenges Arising From Digitalisation – Report On Pillar One Blueprint" dtd 12 October 2020, taxes on profits from the extraction of a nation's natural resources can be considered to be part of the price paid by the exploiting company for those national assets, a price which is properly paid to the resource owner.

[9] The rationale for exclusion of the Financial Services sector from the Pillar 1 proposal stems from the highly-regulated nature of FS business. However, it should be emphasised that this central rationale is not premised on the mere fact of regulation but rather is based on the effects of that regulation. More specifically, the regulations governing the relevant business in each of these three sectors, generally require that appropriately capitalised entities are maintained in each market jurisdiction to carry on business in the market concerned. Due to this factor, the profits that arise in a particular market jurisdiction will generally be taxed in that market location with the result that there is no further need for re-allocation.

[10] Defined as profit in excess of 10% of sales/ revenue of MNE

corresponding modifications to PE rules are made in the tax treaties, the cross border business profits will continue to be taxed as per the existing treaty rules".

- However, given the fact that taxpayers fall within the ambit of the source rule within the Act, the Tax Authorities may insist that such taxpayer should comply with various procedural requirements of the Act, such as obtaining PAN, filing return of income, etc. Any such measure merely increases compliance burden for NR entities, adversely impacts 'ease of doing business' with India and provides no revenue benefit to India – except, perhaps statistical information of revenues flowing from India which is already available from alternative sources like foreign remittance filings by banks.

Recommendations

- To avoid unwarranted compliance burden for NR entities, it may be explicitly provided that the taxpayers from treaty jurisdiction who remain completely outside the scope of the extended nexus rule will not be required to undertake procedural compliances under domestic law (say, obtaining PAN, filing ROI, withholding obligations, etc.).

Guidance should be provided on determination of "users in India" w.r.t user linked condition

Issue

(i) Under the User-linked condition above, SEP is determined basis number of users in India. However, ascertaining the number of users is complex and volatile having regard to differing features and level of participation by users in different types of apps/websites.

Recommendations

For determining the user threshold of 3 lakh users, it is recommended that sufficient guidance be provided for various industry segments to deal particularly with the following illustrative aspects:

- The guidance must comprehensively deal with scenarios such as repeated use by the single user, multiple accounts by single user, fake accounts or fake information provided by users etc.
- Transient users such as tourists must be excluded while determining "users in India".
- Only "active users" should be considered while determining user threshold, since it is mostly the data pertaining to user preferences/behaviour of such active users, which create a value for businesses
- Guidance about determination of location of the user in India should also be provided. For example, as per erstwhile EU directive on significant digital presence, location is determined by reference to the Internet Protocol (IP) address of the user's device or, if more accurately possible, by any other method of geolocation.

- To even out the fluctuations and to capture meaningful and regular presence, annual average of daily/monthly active users may alone be considered as the basis for determining fulfilment of the User-linked condition.
- For this purpose, it may also be clarified that the active users will be determined as per the applicable industry parlance and with particular reference to data which may be published by the business for regulatory and other purposes.

Clarify that certain websites/apps which are not interactive from the scope of SEP

Issue

- As discussed above, user linked condition will create SEP of NR in India if it engages in interaction with prescribed number of users in India. Interaction is generally understood as two-way communication and hence, in some scenarios it is possible that a non-resident has a website (providing generic information about the non-resident) but such non-resident does not engage in interaction through the website. Thus, distinction may need to be drawn between passive websites and interactive websites or mediums.
- As illustrated in BEPS Action 1, interactive websites can include those which allow users to create a personalised account and utilise the local payment options offered on the site for concluding transactions electronically on the website and in such cases there is a clear link between revenue of non-resident and users in source country.

Recommendations

- Even assuming there are merits to keep the user-Linked condition, it may be clarified that websites which are merely accessed by Indian users for information like corporate websites, Wikipedia, product/service information, etc without creating any user account or conducting any financial transactions are not covered under SEP. Since such websites do not store any user information which can be monetised, there is sufficient rationale for keeping them out of scope of SEP.

Clarify that income which is otherwise chargeable under other provisions of the Act should be understood as being outside the scope of SEP

Issue

- It is possible that there is an overlap between SEP provisions and other provisions of the Act such as provisions of interest/ royalty/ FTS under S. 9(1)(v)/(vi)/(vii). It is well settled judicially that specific provision prevails over the general provision.
- Clear distinction needs to be drawn between taxpayers who carry on their business digitally and/or those who are players of the Digital Economy, as distinguished from those who may support the Digital Economy from at a distance. For example –
  - A service provider to a digital player may continue to earn fees for services as before
  - The hirer of the facility will continue to earn rent income and hence royalty income as before

- Grant of IP license by content owner to the licensee for exploitation through digital means is royalty taxable at par with royalty taxable for grant of IP license for exploitation in physical world

- The new provision is apparently not meant to create any different tax treatment for such business enterprises who are otherwise covered by specific charging provisions of the Act.
- For instance, interest which is taxable at concessional tax rate @ 5% u/s. 194LC should not be covered by SEP

Recommendations

- To avoid unintended litigation and in the interest of clarity and certainty, it should be provided that any revenue which is otherwise considered to be chargeable as per any other provision of law should be understood as being outside the scope of this newly introduced SEP provision. For example, if any part of the revenue comprises of royalty income or FTS income, or the like, which is covered by special provisions, the same should be kept out of the revenue base as also the attribution base under Explanation 2A.
- Thus, no part of the revenue which is hitherto considered chargeable to tax should be considered within the net of new taxation policy. The principle will hold good even if such income were to be considered non-taxable by reason of an exemption under the domestic law or by reason of a provision of treaty, etc. For example, fees for technical service should be kept out of the attribution base even if the technical service fee may not be actually subjected to tax since the treaty is operating on the principle of included services (or 'make available' clause).

Clarify the year in which NR triggers SEP where buyer makes advance payment but sale takes place in separate financial year

Issue:

- SEP of NR is triggered where any transaction in respect of any goods, services or property is carried out by a NR with any person in India if the **aggregate of payments arising from such transaction or transactions during the previous year** exceeds INR 2 crore
- In business transactions**,** it is common phenomenon for buyers to make advance payment (say in year 1) and the sale or service transactions takes place subsequently (say in year 2). In such case, where advance payment made in year 1 exceeds INR 2 crore, doubts arise whether SEP triggers
    - in year 1 when advance payment is received by NR, or
    - in year 2 when sale transaction takes place, or
    - both year 1 and 2

- Out of the above options, it may be improper to trigger SEP qua the same transaction in two different years.

Recommendation:

- Explicitly clarify that where payment is made in advance and transaction takes place in subsequent financial year, SEP triggers only in one year either in year of payment or year of sale/service – more preferably, in the year of sale/service.

Relieve obligation of payers as withholding agents and/or representative assessee

Issue

- Predominantly large part of the revenue generated by business players are B2C transactions such that there are millions of users/ customers and each of the user/ customer contributes to a moderate amount of the revenue earned by the business enterprises. The user base is relatively wide, comprised of people of all ages and educational / economic background and from all corners of the geography.
- The present tax withholding provisions, if applied in a strict sense, all the users/ customers who contribute to revenue of business enterprises, which is chargeable to tax under the Act will be required to withhold taxes and comply with related procedures. It can include even payers who would have carried out a small transaction, of say Rs 100, to have monthly subscription of online content.
- It would be extremely onerous to expect such users/ customers of moderate means to comply with the tax withholding provisions and/or to expect them to be treated as representative assessees on behalf of non-residents. The sheer scale of customer base (considering the India population) and the model of business world may require that the recovery and collection model cannot be at par with conventional recovery and collection model. The difficulty multiplies in case of user linked condition wherein payment is not a pre-condition.
- Further, the cost incurred by revenue officers targeting the withholding non-compliance and also catching hold of representative assessee is likely to be not commensurate with the benefit one may derive due to deployment of additional force, tracking every order, every customer etc.
- BEPS Action 1 also states that in the case of B2C transactions requiring withholding from the payer would be more challenging as private consumers have little experience nor incentive to declare and pay the tax due and moreover, enforcing the collection of small amounts of withholding from large numbers of private consumers would involve considerable costs and administrative challenges. The relevant extracts from BEPS Action 1 are:

  "In the case of B2C transactions, however, requiring withholding from the payor would be more challenging as private consumers have little experience nor incentive to declare and pay the tax due. Moreover, enforcing the collection of

small amounts of withholding from large numbers of private consumers would involve considerable costs and administrative challenges."

- The report also acknowledged that one possible solution in such B2C cases would be to require intermediaries processing the payment to withhold taxes.[11] The difficulty in collecting levy in B2C transactions and hence, equipping payment gateways for tax collection is also recognised in EL Report[12]. However, any such administrative mechanism will require creation of suitable infrastructure but will be essential for simplified and consistent implementation of any such novel levy having wide scale impact. This also highlights that till such time a country is ready with suitable infrastructure, the implementation may need to be deferred to a later date.
- Litigation on TDS default has consequential liability as an assessee-in-default as also has interest and penal consequences. Disallowance of expenditure particularly when the quantum of profit attribution is uncertain can have significant tax impact for the payer.
- There is also an apprehension about possible coverage of multiple of small customers within the scope of S.163, if trigger of SEP is regarded as trigger of business connection and/or an opportunity of earning income directly or indirectly from such customers or users in India. While the exposure u/s. 163 cannot be beyond the amount which is earned through a particular customer, it only highlights uncertainty and possible risk of litigation.

Recommendations

- In the initial years of SEP, the provisions may be implemented and enforced only against the primary taxpayer and there should be general notification under S.197A(1F) that provisions of Chapter XVII B will not be made applicable to the payments which may get covered by provisions of Explanation 2A to S.9(1)(i). In any case, such notification must cover those payees which are covered by treaty jurisdictions and it is clear that provisions do not apply to them till there is a suitable treaty modification.
- Without prejudice to the above, a mechanism along the lines of provisions of S.195(3) may be introduced for the payees such that there is ring fencing of the TDS obligation and certainty of implementation from the perspective of the payers.
- In addition thereto, the following carve out may also be provided:
    - In view of onerous obligation on small users in case of B2C, it is recommended that the primary as also the secondary tax liability of collection should be squarely on the recipient of the income and the payer should be relieved completely of its obligation as a withholding agent or representative assessee irrespective of whether the payee is from treaty jurisdiction or non-treaty jurisdiction.

[11] Para 297 of BEPS Action 1 report (2015)

[12] Para 162 of "Committee on Taxation of e-Commerce" which recommended introduction of EL

- Further, in case of B2B transactions, a threshold of INR 10 million may be prescribed such that in those B2B cases, the payer may be required to withhold taxes only when estimated aggregate payments exceeds INR 10 million.

Separate cell for dispute resolution or redressal of SEP cases

Issue

- Considering the complexity and various issues involved in this novel subject, it is essential that the disputes are resolved in an expedited manner or an advance ruling basis by a panel which is comprised of and involves presence of subject specialist.

Recommendations

- A separate cell or bench or panel should be constituted to tackle disputes dealing with SEP similar to Approving Panel entrusted with review of GAAR proposals or designated panel for Advance Pricing Agreements (APAs). It can also be a separate dedicated panel from newly constituted Board for Advance Rulings (BAR). However, any such mechanism should be an alternative to existing mechanisms and optional for taxpayers. It should issue clarifications or pronounce rulings in a time bound manner.
- There should be a highly effective panel which is not only knowledgeable but is independent. The panel may comprise, amongst others, of a business and technology expert.

Introduce specific profit attribution rules for NR triggering SEP in India in lieu of powers taken by board under Section 295

Issue:

- The current profit allocation principles are strongly rooted in physical presence requirements. The principal focus of the existing tax framework is to align allocation of income with the location of tangible or physical economic activities undertaken by the enterprise, including the significant people functions and infrastructure deployed on production/supply side of business. The need to depart from traditional profit attribution rules is acknowledged not only in BEPS report but also in EL Report which evaluated alternatives from India perspective
- Raw customer data, in itself does not result in any value creation and there is, if at all, very small weightage which can be assigned to such raw data. Data can have value to an enterprise only if it is aggregated and structured in a way that the analytical tools deployed by the enterprise can determine relationships among the individual data points. That value is created solely through the development and deployment of the enterprise's platform and data base analytics tools, which in most cases is located outside India. Also, the R&D efforts relevant to such tools involve huge cost and risk. Hence, careful study and sufficient weightage from different factors such as high entrepreneurial risk, large capital, long maturity period, infrastructure, artificial intelligence, software, research and development and innovative skill and significant

people functions of business may be relevant to be undertaken before reaching to any approach

- Any profit attribution approach adopted for SEPs would have to acknowledge that huge losses – particularly in initial years - can be attributed to the SEP. In fact, many digitalized enterprises sustain losses for many years, as they seek to establish a stable market presence. There would need to be explicit guidance on the attribution of such losses, including the prescription of a rule which, in a transit year, recognises all accumulated losses to date for prior years
- Any global formulary approach will be contrary to ALP principles and revenue linked presumptions levy often has vice of being passed on to customers
- Risk of double count of income attributable under clause (a) and (b) of Explanation 2A needs to be eliminated

Recommendations:

- The existing principles/ rules relating to profit attribution to business connection would need to be modified substantially before they can be applied in a meaningful manner to determine profits attributable to a SEP. The modification will require evolution of norms of assessing value contribution of certain features of highly digitalised business models.
- The rules for allocating profits to a SEP should be built on the current transfer pricing framework based on the arm's length principle by treating the SEP as a separate and independent activity for the purpose of identifying assets used, functions performed and risks assumed, adapted suitably to include attributes of digital business.
- Raw data in itself may not be valuable hence, careful and proper weightage needs to be given to consumer data while attributing profits
- The transfer pricing framework would need to be adapted in a consistent manner to reflect the way value is created in digital activities. For instance, the functional analysis of a SEP, while one may consider the relevance of raw data and users, it also needs to take into account role played by factors like high entrepreneurial risk, large capital, long maturity period, infrastructure, research and development and innovative skill and significant people functions of business and has to suitably dovetail risk of such factors borne overseas.
- **Exclusion needed for loss making entities and/or the entities which do not earn income from third parties; 'one size fits all' approach is unlikely to work**
  - Business models in digital industry are peculiar. While the digital world is highly innovative, the rate of technological obsolesce is also very high and many players who are unable to keep up with such pace of innovation fade quickly in this fast paced digital market. Accordingly, the guidance on attribution needs to carefully consider such features and peculiarities of loss making enterprises, obsolescence risk, prospects of loss of loyalty etc.

- Further, while data and user interaction may be relevant, it may be noted that these inputs do not contribute to income or profits until they are monetised. Also, revenue covered by (a) should not be again attributed to activities of clause (b). Further, the headcount of users will need to exclude such users who have contributed to earning of revenue.
- A key element of the business model of many digital firms is that they first aim at rapid growth by creating a large user base, even if this does not initially generate much revenue or profits. This only highlights the need for a nuanced approach while dealing with this issue rather than trying to develop a "one-size-fits-all" model. More specific guidelines on the allocation of profits would need to be developed to provide clarity and certainty.

- Adoption of global formulary approach or presumptuous basis of taxation is contrary to ALP principles and also has vice of being passed on to the customers as transaction cost. Unlike indirect tax levy, such cost does not provide input credit to the customer and enhances the cost of business.

6.2 General Anti Avoidance Rule - Chapter X-A

GAAR provisions should not apply when a tax treaty contains the Principal Purpose Test (PPT)/ Limitation of Benefit (LOB) clause

The FAQ's issued by CBDT on 27 January 2017 while dealing with the question on whether

GAAR would be applied to deny treaty eligibility in a case where there is compliance with (Limitation of Benefit) LOB test of the treaty, clarified as follows

Adoption of anti-abuse rules in tax treaties may not be sufficient to address all tax avoidance strategies and the same are required to be tackled through domestic anti-avoidance rules. If a case of avoidance is sufficiently addressed by LOB in the treaty, there shall not be an occasion to invoke GAAR……(emphasis supplied).

Whether the case of avoidance has been sufficiently addressed may further involve an element of subjectivity as the term 'sufficiently addressed' has not been explicitly defined and there could be an unintended situation where the case would be subjected to both the rigors of the anti-abuse provisions as well as GAAR.

It should be provided by way of an exception that when an arrangement/transaction is subjected to the anti-abuse provisions [particularly the LOB and PPT provisions] dealt with by the tax treaty between India and the respective country, the same should not be further subjected to GAAR provisions.

Overlapping of the GAAR provisions with the anti-abuse provisions introduced through the Multilateral Instrument

India has signed the 'Multilateral Instrument' (MLI) in accordance with the BEPS Action Plan 15 of the OECD, which, inter alia, deals with the denial of tax treaty benefits in certain cases of anti-abuse arrangements/transactions entered into by the taxpayer. The MLI provides for insertion of anti-abuse provisions (the PPT and the LOB provisions) in the tax treaties so as

to deny tax treaty benefits in case of abusive arrangements/transactions being entered into by the taxpayer. The anti-abuse provisions inserted through the MLI would be effective once the same are ratified by both the signatories to the MLI. With India having signed the MLI, there could be a possibility that the same transaction/arrangement could be subjected to multiple anti-abuse provisions, one would be through the anti-abuse provisions inserted in the tax treaty network through the MLI and second by way of the same transaction being subjected to the GAAR provisions which also targets anti-abuse provisions.

It is suggested that GAAR provisions should not be made applicable to abusive transactions (in the case of Multinational enterprises {MNE's}) which are subjected to anti-abuse provisions under the tax treaty pursuant to the adoption of the MLI provisions. Once the anti-abuse provisions are inserted in the respective tax treaties through the MLI, the government could then assess the situation and examine if GAAR provisions should be made applicable in the case of the said non-resident taxpayers' (MNE's). This would also pave the way for a conducive economic environment and persuade the global multinationals to establish their footprint in India with clarity on the domestic tax laws prevalent in the country.

Further, it should be clarified that the provisions of Multilateral Instrument (for instance, the Principle Purpose Test) should not be resorted to in order to take away the benefit of grandfathering granted under Rule 10U (in respect of income from transfer of investments made before 1 April 2017).

Further, it is recommended that suitable safeguards (similar to those present in GAAR provisions) should be put in place for invocation of PPT. This will alleviate the widespread concern of the taxpayers that PPT will be invoked by the tax authorities without satisfying the checks and balances as provided in the GAAR provisions.

The meaning of the terms 'Substantial' and 'Significant' in Section 97(1) of the Act

Section 97(1) of the Act provides that an arrangement shall be deemed to be lacking commercial substance, if inter alia;-

- it involves the location of an asset or of a transaction or of the place of residence of any party which is without any <u>substantial commercial purpose</u> other than obtaining a tax benefit for a party; or
- it does not have a significant effect upon business risks, or net cash flows apart from the tax benefit.

  The terms 'substantial commercial purpose' and 'significant effect' in the context of GAAR have not been defined in the Act.

Recommendations

- It needs to be clarified what shall constitute as "substantial commercial purpose' and "significant effect' for the purpose of section 97 of the Act.
- Substantial commercial purpose may be explained with reference to the terms used viz. location of an asset/transaction or place of residence of a party (for e.g. specified value

of assets located; value of a transaction as comparable to the total assets of the business or any other such related parameter).

- Similarly, what will constitute as 'significant effect' vis-a-vis business risks/net cash flows needs to be clarified.

Clarification on the term 'tax benefit' as defined under section 102(10) of the Act

The term 'tax benefit' as defined under section 102(10) of the Act includes,—

> *"(a) a reduction or avoidance or **<u>deferral of tax</u>** or other amount payable under this Act; or*
>
> *(b) an increase in a refund of tax or other amount under this Act; or*
>
> *(c) a reduction or avoidance or deferral of tax or other amount that would be payable under this Act, as a result of a tax treaty; or*
>
> *(d) an increase in a refund of tax or other amount under this Act as a result of a tax treaty; or*
>
> *(e) **<u>a reduction in total income; or</u>***
>
> *(f) **<u>an increase in loss,</u>***
>
> *in the relevant previous year or any other previous year;"**(Emphasis supplied)***

Clause (e) and (f) in the definition refer to "reduction of total income" and "increase in loss" as tax benefit. An ambiguity arises as to how tax benefit is conditioned at income/loss level. This may also defeat the objective of Rs. 3 crore tax benefit threshold as provided in Rule 10U of the Income-tax Rules, 1962 (the Rules).

Computation of tax benefit on deferral of tax (which is merely a timing difference) needs to be clarified. As observed by the Expert Committee[13], in cases of tax deferral, the only benefit to the taxpayer is not paying taxes in one year but paying it in a later year. Overall there may not be any tax benefit but the benefit is in terms of the present value of money.

Further, as observed by the Expert Committee (Page 47 of the Final Report by the Expert Committee on GAAR chaired by Dr. Parthasarathi Shome), the term tax benefit has been defined to include tax or other amount payable under this Act or reduction in income or increase in loss. The other amount could cover interest.

Recommendation

Clause (e) and (f) should be appropriately worded to correspond with the 'tax' amount. In other words, the reference to income/loss should not be the base for defining the term 'tax benefit'.

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[13] Page 48 and 49 of the Final Report by the Expert Committee on GAAR chaired by Dr. Parthasarathi Shome.

In line with the Expert Committee recommendations, it is suggested that the tax benefit should be computed in the year of deferral and the present value of money should be ascertained based on the rate of interest charged under the Act for shortfall of tax payment under section 234B of the Act.

6.3 Place of Effective Management

The pertinent issue with respect to place of effective management is summarised below:-

Issue and Recommendation

- Given the language used, CBDT Circular No. 25/ 2017 dt 23 Oct 2017 may be interpreted as being applicable only to cases where the role played by the Indian Regional headquarters (RHQ's) employees are in relation to day-to-day or "routine" functions (and that too only if further the foreign company fulfills the Active Business Outside India test). Hence, where highly talented and senior Indian employees of RHQs perform not just a routine function but also participate in senior management functions like strategic or commercial decision-making activities, there is a risk of POEM being held to be in India, despite the Circular. Thus, it is requested that a suitable legislative amendment or specific clarificatory Circular be issued clarifying that the purpose of the POEM guidelines is not to capture income earned by the overseas entities of Foreign Multinational Group Companies or to tax in India their income from operations outside India, merely on the ground of certain employees of the Indian subsidiary having a regional role and multi-country responsibility or oversight over the operations in other countries of the region.
- The clarification will be in line with the very intent for which the POEM guidelines were introduced, i.e. to target Indian groups having shell companies outside of India.

6.4 Equalisation Levy

The Finance Act, 2016 introduced a levy of tax (termed as Equalisation Levy) on certain specified services. Equalisation Levy shall be 6% of the amount of consideration for specified services received/receivable by a non-resident (not having a Permanent Establishment in India) from (a) a person resident in India or (b) a non-resident having a PE in India.

Issues

- The levy is applicable to payments made for, *inter alia*, 'online' advertisement. The term 'online' has been defined to include facility/service etc. obtained through the internet or any other form of digital or telecommunication network. The scope of the term 'online' appears to be wide and could possibly even cover advertisements placed on foreign television channels.

Recommendations

- Enabling provisions to allow non-residents to claim refund of the levy, non-applicability of the levy, appeals, etc. should be introduced in the Chapter VIII.
- Enabling provisions be introduced to facilitate non-residents having losses, to apply for nil/lower equalization levy certificate. Payer should be granted a mechanism to apply to

the local tax officer to determine whether the transaction is subject to Equalisation Levy or withholding tax provisions under the Act. Accordingly, payer should be allowed to make an application to the tax officer in advance for determining whether it should deduct Equalisation Levy or withholding tax at appropriate rate.

- It is requested that the abovementioned issues on the applicability of levy on revenues received from advertisements placed in foreign television channels. be clarified by the Government.
- Specific provision be introduced for appeal to be made against intimation of processing of annual statement of equalization levy.

Section VII

Issues related to allowability of Certain Expenditure, Deductions and Disallowances

7.1 Allow deduction for Corporate Social Responsibility Expenditure – Section 37 Issues

- One of the highlights of the Companies Act, 2013 is that every company meeting the specified threshold would need to mandatorily spend 2% of their 'average net profits' on Corporate Social Responsibility (CSR).
- As per amendment made by the Finance (No. 2) Act, 2014, the expenses incurred by the taxpayer on the activities relating to CSR referred to in Section 135 of the Companies Act, 2013 shall not be deemed to be incurred for the purpose of business and hence, shall not be allowed as a deduction under Section 37(1) of the Act.
- The corporate sector spend is effectively assisting the Government in undertaking social projects for the country. Therefore, making an express provision for not allowing a deduction is unfair. Even if deduction is allowed, it means that 66% of the cost is anyway being borne by the contributing corporate entity. The expenditure incurred during such difficult time during COVID-19 Pandemic, by corporates should be motivated.

Recommendation

- It is recommended that the Explanation 2 to section 37 of the Act should be omitted and a deduction of CSR expenses incurred by the taxpayers pursuant to provisions of the Companies Act should be allowed under section 37 in computing business income.

7.2 Depreciation – Section 32 - Provide clarity in respect of person who can claim depreciation on leased assets under operating lease, finance lease, sale and lease back etc., provide higher rate of depreciation on plant and machinery, Extend benefit of additional depreciation under section 32(1)(iia) to service industry

Issues

There is no clarity on allowability of depreciation on finance lease transaction. In various judicial precedents it is been upheld so long as the transaction is accepted to be a 'lease' and not a 'loan', the lessor should be entitled to depreciation regardless of whether the lease is classified as 'operating lease' or 'finance lease' in books. But in absence of clear & objective guidance to distinguish between a 'loan' and 'lease' transaction, litigation has continued on allowance of depreciation to lessor. In some cases, depreciation has been denied to both lessor and lessee. Suitable legislative clarifications in this regard would go a long way to minimise litigation and providing certainty to the taxpayers.

- Allowability of depreciation on toll rights in Build, Operate and transfer (BOT) projects in roads. CBDT Circular No. 9/2014 dated 23 April 2014 states that while no depreciation can be allowed since toll road does not belong to the BOT operator, the taxpayer is entitled to amortised deduction over the toll period. An option be provided to the

taxpayer to either claim depreciation as "intangible asset" or claim amortised deduction as per the aforesaid circular.

- Current depreciation on plant and machinery @ 15% is too low. Need for Higher depreciation for plant and machinery.
- Hotel Buildings constitute the 'plants' for the hotel industry as their usage is round the clock for 24 hours. The industry has to make very heavy investments in renovation, upgradation and upkeep of the hotel buildings. Section 32 of the Act should therefore be amended to restore the depreciation rate to 20%.
- The main revenue generating asset of any Hospitality Industry i.e. a Hotel, essentially relates to its property - buildings. Though the Act had granted certain relief on profits generated by Hotels set up in a backward State with the intention of improving Tourism, no benefit is extended to existing Hotels including Heritage Hotel buildings, which needs continuous updation and construction. Due to various local laws and the laws relating to Heritage buildings several Hotels have to undertake various construction and strengthening projects which ensures the compliance of various laws. However this is only at the cost of stopping the business for the entire hotel or a section thereof. However, such hotels do not get any benefit in taxation and it takes quite a number of years to recoup the cost of capital and investments. It is recommended to allow additional or accelerated deduction from business profits on preservation of Heritage Hotels on entire civil construction expenditure.
- The accelerated depreciation ranging mostly between 80-100% was available for certain block of assets such as renewable energy devices, air pollution control equipment, energy saving devices, etc. upto AY 2016-2017. CBDT vide notification no. 103/2016, dated, November 7, 2016, has restricted the highest rate of depreciation to 40% with effect from 1 April 2017. The accelerated depreciation on assets like computers, computer software, renewable energy devices, air pollution control devices, energy saving devices etc. was provided not as an incentive but considering their fast obsolescence due to rapidly changing technology. Accordingly such accelerated depreciation on environment saving/friendly devices should be retained. Further, such restricted rate should be made applicable only to the new assets acquired on or after 1 April 2017. At the very least, the highest rate of depreciation should be fixed at 60%. It should also be clarified that in respect of taxpayer who may have qualified for higher rate of depreciation (but, in whose case, the depreciation relief was restricted to 50% since the asset was acquired in the latter half of the year) the taxpayer should be permitted to avail the balance depreciation as per old rates with regard to the unabsorbed portion.
- Additional depreciation under section 32(1)(iia) of the Act is currently not available to service industries.
- Whether 'non-compete fee' can be regarded as 'any other business or commercial right of similar nature', to be eligible for depreciation as 'intangible asset' under Section 32 of the Act.

Recommendations

- The Government should provide clarity in respect of person who can claim depreciation on leased assets under operating lease, finance lease, sale and lease back and other financing arrangement by laying down objective rules.
- It is requested that it may be specifically clarified that right to collect toll or charges or annuity for using infrastructure facility is an 'intangible asset' and allow depreciation under the Act consistent with accounting treatment as per Companies Act. Further, an option be provided to the taxpayer to either claim depreciation as "intangible asset" or amortised deduction as per the Circular No. 9 /2014 dated 23 April 2014.
- It would be in fitness of things to restore the rate of depreciation on general plant and machinery to 25% from 15% to encourage investment in new plant and machinery entailing up-gradation of obsolete technologies. This would also provide an impetus to the manufacturing sector.
- The Government should extend the additional depreciation under Section 32(1)(iia) of the Act to service industries as well which is currently available to only manufacturing sector.
- There is a lack of clarity as to whether payment made for non-compete fees shall be eligible for depreciation under Section 32 of the Act as 'intangible assets', which has given rise to unintended litigation. It is therefore, suggested that a clarificatory amendment should be made in Section 32(1)(ii) of the Act to include non-compete fee within the definition of 'intangible asset'.

7.3 Allow Payment of Premium of Leasehold Land as a Revenue Expenditure

Under the Ind AS 16, the upfront premium paid on leasehold land held under operating lease are being treated as prepaid expenses and would need to be charged to the Profit and Loss statement under the head "rentals" on a proportionate basis over the life of the lease period.

These upfront lump sum premium lease payments for leasehold land are essential business expenditure and do not generate any capital asset and hence are purely revenue in nature.

These are just like payments made under any operating lease to utilise the leased property for the purposes of the business of the lessee and hence should be allowed just like any business expenditure for tax purposes.

Recommendation

Appropriate clarity should be provided to the effect that upfront premium payments for leasehold land, shall be allowed as deductible expenditure under the Act in the year of its debit to the statement of Profit and Loss.

7.4 Amend Rule 103 of the Rules to provide flexibility in ordinary annual contribution to approved fund by the employer as per the actuarial valuation

Issue

AS-15 requires that provision for gratuity should be made on the basis of actuarial valuation which is a scientific method of computing estimated liability by considering various

yardsticks such as length of service, salary progressions, rate of discounting, age of employee etc. Section 40A (7) of the Act provides for deduction of provision made for contribution to an approved Gratuity fund. However, Rule 103 of the Rules restricts the ordinary annual contribution to 8.33 per cent of the salary of each employee during each year.

Gratuity payable on the balance sheet date as per Actuarial Valuation most of the times exceeds the 8.33 per cent of the current salary of an employee as the same is computed based on various factors considering period of length, increase in salary, retirement age, mortality, discounting rate etc. However employer does not get deduction for the payment to an approved gratuity fund more than 8.33 per cent of the salary of each employee. This restriction acts as deterrent to contribution to approved Gratuity fund.

Recommendation

It is recommended that Rule 103 of the Rules be amended to provide flexibility in ordinary annual contribution to approved fund by the employer as per the actuarial valuation.

7.5 Allow 100% Head Office Administrative Expenses in case of non-residents – Section 44C

Issue

- Section 44C of the Act provides restriction for deduction of head office expenditure in case of non-residents to the extent of 5% of the adjusted total income.

Recommendation

- It is recommended that 5% cap on deductibility of Head Office Administrative Expenses as provided in section 44C of the Act should be removed and deduction may be allowed based on arm length principles and transfer pricing provisions.

7.6 Issues related to taxability of subsidy/grant/incentive/drawback, etc.

Issue

The Finance Act, 2018 introduced Section 145B(3) in the Act, which provides that income referred to Section 2(24)(xviii) 6 of the Act shall be deemed to be the income of the previous year in which it is received, if not charged to income tax for any earlier previous year.

The income referred to in Section 2(24)(xviii) of the Act dealing with government grants, subsidy, duty drawback, etc. is to be taxed in the year in which it is received.

When a government gives a grant, the right to receive the grant is bestowed upon the taxpayer upon satisfying certain conditions linked with the grant which generally are to be satisfied in the subsequent years. The income in such a situation would accrue not only when it becomes due but it must also be accompanied by a corresponding liability of the other party to pay the amount.

The result of the amendment is that the year in which the government grant is taxed in the hands of the taxpayer may be different from the year in which the said entitlement ultimately becomes due to the taxpayer upon satisfying of the linked conditions in the

subsequent year and consequential corresponding liability of the third party. The relevant provision of Section 2(24) is reproduced below:-

> 2(24) assistance in the form of a subsidy or grant or cash incentive or duty drawback or waiver or concession or
>
> (*xviii*) reimbursement (by whatever name called) by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee *other than,—*
>
> (*a*) *the subsidy or grant or reimbursement which is taken into account for determination of the actual cost of the asset in accordance with the provisions of* Explanation 10 *to clause* (1) *of section 43; or*
>
> (*b*) *the subsidy or grant by the Central Government for the purpose of the corpus of a trust or institution established by the Central Government or a State Government, as the case may be*

It is possible that the taxpayer may not satisfy the conditions in the future that are linked to the bestowing of the grants. If the conditions that are linked to the grant are not satisfied, the grant may be withdrawn resulting in taxing the receipt/grant in the earlier years which is actually not received by the taxpayer. This would result in an anomaly leading to a situation where the grants are taxed in an earlier year whereas the grant bestowed on the taxpayer has been withdrawn subsequently.

Recommendation

It is thus suggested that the grants received by the taxpayer should be taxed when the amount corresponding to the grant becomes due upon satisfying of the conditions linked to the grant and it must also be accompanied by a corresponding liability of the other party to pay the amount. This would also be in line with the general principles of accounting discussed by the Supreme Court in the case of CIT v. Excel Industries[14].

[14] CIT v. Excel Industries Ltd. 358 ITR 295 [SC] (2013)

Section VIII

Non-resident, Mergers and Acquisitions, Capital gains, Transfer Pricing and Tax Deducted at Source related Issues

8.1 Non-Resident related provisions

8.1.1 Amend Rule 29 of the Rules to permit Non-resident shareholders of private companies to obtain Certificates for deduction of income-tax at DTAA rate or lower rate or no deduction of income tax

Dividends received on or after 1 April 2020 are now taxable in the hands of shareholders.

In case of non-resident shareholders, dividends are taxable at 20 per cent on gross basis under section 115A of the Income-tax Act, 1961 ('the Act'). However, most Indian tax treaties provide for taxing dividends at a rate lower than the rate prescribed under section 115A – typically, ranging from 5 to 15 per cent. This represents the final tax liability with respect to dividends in the case of non-resident shareholders.

Under section 195 of the Act, tax is deductible at source by the Indian company paying dividends to a non-resident shareholder at the rates in force. Accordingly, in terms of section 195 read with section 2(37A)(iii) of the Act, an Indian company paying dividends can withhold tax at the treaty rates. For the said purpose, treaty eligibility of the non-resident shareholder will have to be evaluated by companies paying the dividend before withholding tax at the lower rate provided under the tax treaty.

Given the complexities involved in determining the treaty eligibility, and significant ramifications for the payer for any alleged non-compliance with withholding tax provisions, companies paying dividend may need certainty as to the eligibility of shareholders to claim treaty benefits.

Issues

- Section 197(1) of the Act provides that the recipient of income can make an application to the Assessing Officer ('AO') for deduction of tax at lower rates or non-deduction of income-tax. The AO, on being satisfied with the claim of the recipient, can grant him such a certificate as may be appropriate. Section 197(2A) further provides that the cases and circumstances under which an application can be made for grant of the certificate will be specified in the rules made in this regard.

  In the context of dividend income, Rule 29 inter alia provides that only shareholders ***holding shares in public companies*** can apply for a certificate for deduction of income-tax at rates lower than 'rates in force' or no deduction of income tax.

- Rule 29 was introduced over 50 years ago - at a time when cross-border investments were limited. Since the liberalization of the Indian economy in 1991, foreign investment has seen a steady and significant growth. The government continues to take various regulatory and tax measures to attract foreign investment. Thus, in today's investment environment which comprises of substantial investment through non-residents investors, there is a need to provide certainty to the non-resident shareholders ***holding***

shares in private companies also, at the stage of withholding itself and provide comfort to the companies paying dividend that they have appropriately complied with the provisions of withholding taxes – more particularly, considering that they also run the risk of being treated as 'representative assessee' under section 163(1)(c).

- For non-resident shareholders, the withholding tax under section 195 is the final tax liability in respect of the dividend income, since the dividend is taxable on gross basis. Enabling non-resident shareholders of private companies to approach the Assessing Officer to obtain a certificate for deduction of tax at source at DTAA rates, will be useful and prevent undue hardship to the non-resident shareholders, who would otherwise have to separately seek a refund for the same.

Recommendations

- In view of the above, we request that Rule 29 of the Rules be expanded in scope to enable non-resident shareholders holding shares in private companies as well. In addition, the rule may also be modified to permit to apply not only for TDS at rate lower than rates in force or nil withholding certificate but also for withholding at DTAA rates. Further, it may also be clarified that where the domestic company has deducted tax at DTAA rate pursuant to certificate issued under section 197, then it will not be treated as 'representative assessee' under section 163(1)(c) of the Act.

8.1.2 Scope of "business connection"- Exclusion provided in earlier clause (a) of Explanation 2 to clause (i) of section 9(1) of the Act for the purchase of goods or merchandise in India should be reinstated

The Finance Act, 2018 has amended the definition of 'Business Connection' to align it with BEPS Action Plan 7 to include any business activity carried out through a person who, acting on behalf of the non-resident has and habitually exercises in India, an authority to conclude contracts or habitually concludes contracts or habitually plays the principal role leading to conclusion of contacts by that non-resident.

Issue

- The amendment has substituted the earlier clause (a) of Explanation 2 to Section 9(1)(i) of the Act. However, on substitution, the exclusion for the purchase of goods or merchandise for the non-resident' appears to be inadvertently deleted. This would result in a significant number of cases where non-residents who are involved only in purchase activities to constitute business connection in India.

Recommendation

- The exclusion provided in earlier clause (a) of Explanation 2 to clause (i) of section 9(1) of the Act for the purchase of goods or merchandise in India should be reinstated.

8.1.3 Issues regarding Indirect Transfer of Capital Asset situated in India

Explanation 5 to Section 9(1)(i) of the Act, which was introduced by the Finance Act, 2012 provides that a share or an interest in a company or entity registered or incorporated

outside India shall be deemed to be situated in India, if the share or interest derives its value substantially from the assets located in India.

The Finance Act, 2015 has amended provisions dealing with indirect transfer of capital asset situated in India. The amendment provides clarity on certain contentious aspects with regards to taxation of income arising or accruing from such indirect transfers. Further, CBDT vide Notification 55/2016 dated June 28, 2016 has notified the Rules prescribing the manner of computation of FMV of assets of the foreign company or entity and relating to the reporting requirements by the Indian concern.

Issues and Recommendations

- There is no clarity on the phrase 'assets located in India' mentioned in Explanation 5 to Section 9(1)(i) of the Act, given that the following interpretations are possible:-
- Whether the section refers to shares of an Indian company as assets located in India; or
- Whether it is referring to the assets owned and held by the Indian company whether in India or outside India.
- Clarification should be provided for the phrase 'assets located in India' mentioned in Explanation 5 to section 9(1)(i) of the Act.
- Intra-group transfers as part of group re-organizations (other than amalgamation and demerger) should also be exempt from the indirect transfer provisions. Suitable amendment should be made in the Act to incorporate relaxations for transfer of minority stakes which do not result in transfer of control of underlying Indian asset, and where the transfer of stake is within the same group, thereby permitting group reorganisation
- Since the objective of the amendment is to tax indirect transfer through shell companies, a listed company should not be considered as a shell or conduit company. The same was also suggested by the Shome Committee.

  It is recommended that indirect transfer provisions must be suitably modified to provide for an additional exclusion from capital gains liability in cases of transfer of shares of foreign companies which are listed and regularly traded on recognized stock exchanges abroad. The criteria for recognition of stock exchanges and for determination of the regularly trading threshold may also be suitably clarified.
- While Explanation 5 to Section 9(1)(i) of the Act provides that shares of a foreign company which derives directly or indirectly its substantial value from the assets located in India shall be deemed to be situated in India, section 47(vicc) of the Act provides exemption only if the shares of foreign company derive substantial value from shares of an Indian company. While the intent may be to exempt all cases of demerger where foreign company derives substantial value from assets located in India, the reading of Section 47(vicc) of the Act indicates that the said exemption would be available only in cases where the shares of the foreign company derive substantial value from shares of Indian company. Due to this inconsistency in the language of Section 47(vicc) vis-à-vis

Explanation 5 to Section 9(1)(i), transfer of shares of a foreign company which derives its value predominantly from assets located in India (other than shares of an Indian company) under a scheme of demerger may be deprived of the aforesaid exemption. Similar inconsistencies also exit in the language of section 47(viab) of the Act.

It is recommended that Section 47(vicc) should be amended to provide that *"any transfer in a demerger, of a capital asset, being a share of a foreign company, referred to in Explanation 5 to clause (i) of sub-section (1) of section 9, which derives, directly or indirectly, its value substantially from the* ***assets located in India,*** *held by the demerged foreign company to the resulting foreign company, if,—………………."* Similar amendment should also be made in Section 47(viab) of the Act (i.e. in case of amalgamation).

- The Finance Act, 2015 prescribes a threshold for applicability for the indirect transfer provisions. There should also be a minimum threshold prescribed for reporting of transactions by the Indian entity. It should be clarified that the same threshold will apply for reporting of transactions under Section 285A of the Act.
- The onus of reporting has been cast on the Indian entity. Generally, the Indian entity may not have information relating to overseas indirect transfer, therefore, the onus of reporting should not be cast on the Indian entity. Considering that the provisions relate to indirect transfers, the onus, if at all, should be cast on the parties to the transaction and not the Indian entity.
- Provisions of Section 234A, 234B, 234C and 201(1A) of the Act should not be applied in cases where demand is raised on a taxpayer on account of the retrospective amendment relating to the indirect transfer. An appropriate amendment should be made in the respective provisions of the Act.

8.1.4 Provide Clarity on Taxability of Offshore Supplies

Supply of heavy machinery and equipment from outside India in capital intensive/infrastructure companies is quite common. It includes supply of equipment, machines, tools, material etc. by a contractor from overseas. In case of offshore supplies, transfer of title in the goods generally happens outside India and the consideration for such supplies is also received by the non-resident contractor outside of India.

There has been significant controversy around taxability of offshore supplies where such supplies constitute part of a composite contract including onshore supplies and services. The tax authorities in such contracts allege that since offshore supply is part of the composite turnkey contract, income from such supplies should also be taxable in India.

Issue

Considering the definition/meaning of offshore supplies is not provided in the statute, the term is subject to wide and varied interpretation. Judicial precedents (including the Supreme Court) on this issue have time and again laid down the criteria to be satisfied for a supply contract to be considered as offshore and held that offshore supply is not liable to tax India. Even then the tax officers continue to hold that offshore supplies are taxable in

India. This leads to prolonged litigation with the tax authorities since the matter largely gets settled at the tax Tribunal/Court level.

Recommendation

It is suggested that the Government should issue guidelines in relation to taxability of offshore supplies so that the essential aspects for taxing or making the same non-taxable are clearly spelt out. The Government may consider re-introducing Circular No. 23 dated July 23, 1969 with suitable modifications. This would provide greater level of certainty and help to reduce litigation for the non-resident contractors in India.

8.1.5 Clarification of the Terms 'Transfer of Title, Risk and Reward'

Issue

With changing times, the contracting terms between the parties have evolved significantly. For instance – a contracting structure could exist wherein the offshore supplies are required to be delivered on CIF basis to the Indian customer, even though the transfer of title in such goods happens outside India. Further, there are situations wherein the transfer of risk associated with the supply of goods happens in India, even though the transfer of title in such goods happens outside India.

In the above situations, where one of the events (such as transfer of risk) or some of the ancillary activities such as (inland freight, transportation etc.) happens in India, then the tax authorities hold that the transfer of title in the goods has not happened outside India. In these situations, the authorities tax the entire offshore supplies in India.

Recommendation

It is recommended that clear guidelines keeping the practical aspects should be laid out in relation to transfer of title, risk and reward.

8.1.6 Clarify definition of 'Indian Concern' under section 115A to include Indian branch

Issue

Section 115A(1) of the Act refer to the term 'Indian concern'. However, the said term is not defined. This leads to a controversy on whether Indian branch qualify as Indian concern and thereby whether the provisions of section 115A(1a) and 115A(1b) are applicable to payment made by such Indian branch. As the term is not defined, there may be an unintended tax disadvantage for an Indian branch of foreign entities intending to raise funds through advances/loans or paying fees for technical services/royalties to non-residents, as compared to other entities registered in India.

Recommendation

It is suggested that the definition of the term 'Indian concern' or an explanation that the said term includes 'Indian branch' may be introduced in the provisions of section 115A of the Act.

8.2 Mergers & Acquisitions

8.2.1 Amend Section 115JAA to provide that successors in case of amalgamation, demerger or any other form of reorganization is eligible to claim benefit of MAT Credit

Issues

- MAT credit is akin to advance payment of tax.
- Benefit of MAT credit cannot be denied to successors in case of reorganization. There are rulings in case of Ranganathan Industries Private Limited (Chennai) ITA 2434/Mds/2004, Caplin Point Laboratories Ltd. (Chennai) ITA 667/Mds/2013, Adani Gas Limited (Ahm) ITA Nos. 2241 & 2516/Ahd/2011, SKOL Breweries Ltd. (Mum) ITA 313/Mum/07, wherein it has been held MAT credit can be carried forward by the amalgamated company/ successor company in case of demerger.

Recommendation

- Section 115JAA of the Act should be amended to provide that successors in case of amalgamation, demerger or any other form of reorganization should be eligible to claim benefit of MAT Credit.

8.2.2 Provide credit for TDS and Advance Tax paid by demerged company or amalgamating company

Issue

- Where there is amalgamation or merger or demerger, tax officers deny the TDS/advance tax credit available to the amalgamating/demerged entity in the hands of resulting entity during the course of assessment proceedings.

Recommendation

- Advance tax paid by the demerged company or amalgamating company on behalf of the resulting company or amalgamated company or TDS available to demerged company/amalgamating company should be given appropriate credit.

8.2.3 Need for Amendment in Section 72A - Carry Forward and Set off of Accumulated Losses in Amalgamation or Merger

Issues

- Currently, Section 72A of the Act allows carry forward of loss and accumulated depreciation in case of amalgamation/ demerger of the following type of companies:-
    - a company owning an industrial undertaking or a ship or a hotel with another company,
    - a banking company,
    - one or more public sector company or companies engaged in the business of operation of aircraft.

- Apparently, the benefit is not available to all the companies engaged in the business of providing services. Considering the facts that many multinational companies have entered in the Indian service market and it has become imperative for the small companies to consolidate their resources to survive, the benefit applicable under the provision of Section 72A of the Act should be extended to all companies irrespective of their line of operations.
- The amendment will facilitate smooth operational reorganization across the economy including infrastructure sector if the benefit of this provision is provided to service providers such as Telecom Infrastructure Service Provider (TISP) and Direct-to-Home (DTH) operators etc. Further, e-commerce sector should also be included in this provision as such businesses require acquisition/consolidation for growth and expansion/ diversification.
- More so, section 72A(2) of the Act prescribes stringent condition about continuity of holding of assets by the amalgamating company for at least two years prior to transfer and by the amalgamated company for five years post transfer. Similarly it requires that the amalgamating company should be in the business for at least 3 years prior to the amalgamation. The conditions in the hands of the amalgamated company are sufficient to control misuse of the provisions and therefore, the conditions applicable to the amalgamating company should be deleted. Also, holding of assets and continuation of business for five years is quite a long period.
- As per the provisions of section 72A of the Act, business loss and unabsorbed depreciation of demerged company can be transferred to resulting company on demerger. However, there is ambiguity in relation to the period for which such losses are available to the resulting company.

Recommendations

- Section 72A of the Act should be amended to allow benefit of carry forward of losses, pursuant to amalgamation, to all companies irrespective of their line of business especially services business.
- Section 72(A)(2) of the Act be amended to delete conditions under sub-clause(a) relating to amalgamating company.
- Also, Section 72A(2)(b) of the Act should be amended to reduce the period of holding assets and carrying on of business to 3 years.
- It is recommended to provide that such losses transferred on demerger should be available for a period of eight years after demerger, as in case of amalgamation.

8.2.4 Clarity on Restriction on Carry Forward and Set off of Losses - Section 79

Issue

The extant provisions of section 79 of the Act restrict closely held companies from carrying forward and setting off losses in case shareholding varies by more than 49 percent in the

year in which the loss is considered to be set off vis-a-vis the year in which the loss is incurred.

In the event of a business reorganization by which a holding company transfers the shares of its 100% subsidiary to another subsidiary, the first subsidiary will not be in a position to carry forward and set-off its losses (if any) as there is a 100% change in its shareholding. However, in such a situation, the holding company continues to hold 100% of the shares of the second subsidiary, which in turn holds 100% of the shares of the first subsidiary. There are conflicting decisions of the courts on this issue, one view point is that the immediate change in shareholding should be tested whereas other view point is that the ultimate change in shareholding should be tested, in order to invoke rigors of section 79 of the Act.

Recommendation

It is recommended that necessary clarification be provided by the Government to settle the ambiguity surrounding on this issue by providing that the restriction posed by section 79 of the Act will not apply to intra group reorganization where a holding company transfer shares of its subsidiary to another subsidiary since the ultimate (beneficial owner) remains the same.

8.2.5 Introduction of safe harbour exemption to section 56(2)(viib) of the Act for tax neutral reorganisation

Section 56(2)(viib) of the Act should be amended to provide for omnibus carve out in respect of tax neutral reorganisations like issue of shares on amalgamation, demerger or transfers exempt under section 47(iv)/(v), etc. without the need for the company to separately justify the value to the assessing officer.

8.3 Capital Gains

8.3.1 Provide clarification under section 55(2)(ac) of the Act on grandfathering benefit in case of shares received under tax neutral transfer in lieu of shares held as on 31 Jan 2018

The Finance Act, 2018 reintroduced capital gains tax on transfer of specified long-term capital assets including equity shares of a company listed on a stock exchange at a lower rate of 10% (plus applicable surcharge and cess). While section 55(2)(ac) of the Act has to a large extent ensured protection by grandfathering the gains earned up to 31 January 2018 on such long-term capital assets, ambiguity is being experienced in the following cases:-

a) Where shares of listed amalgamating company were acquired before 1 Feb 2018 and amalgamation takes place on or after 1 Feb 2018, it is recommended that specific retrospective clarification should be brought that shares of listed amalgamated company (though issued after 1 Feb 2018) should be deemed to be acquired from the date of acquisition of shares of the listed amalgamating company for the purposes of section 55(2)(ac) of the Act. Accordingly, Fair Market Value (FMV) of such asset for the purposes of section 55(2)(ac) of the Act should be the highest price of the equity shares of the listed amalgamating company quoted on 31 Jan 2018.

b) Similarly, specific clarification should be inserted that shares of the listed company received by the shareholders under tax neutral transfer under section 47 of the Act shall

be deemed to be acquired from the date of acquisition of the previous owner or assets in lieu of which the shares listed as on date of transfer were acquired, as the case may be.

c) In case of shares of demerged company held on 31 Jan 2018, FMV of shares of demerged company as determined in terms of Explanation (a) to section 55(2)(ac) of the Act should be pro-rated between shares of demerged company and resulting company as per section 49(2C)/(2D) of the Act.

8.3.2 Resolve ambiguities in one-time option under section 54 for availing exemption by re-investment in two residential houses

The Finance Act, 2019 inserted proviso to section 54(1) of the Act to provide a one-time opportunity to the taxpayer to claim exemption under section 54 of the Act with respect to investment in two residential house properties where the amount of long term capital gains does not exceed Rs. 2 crores. However, certain ambiguities arise as under which need to be clarified by the Government to avoid unwarranted litigation.

(a) Where taxpayer deposits the amount in capital gains account scheme and exercises the one-time option, but ultimately he buys only one property, it is not clear whether the taxpayer will be denied deduction under section 54 of the Act on the ground that (as a result of substituted reference), the taxpayer is mandated to qualify for exemption only if he has acquired two houses. Similarly, if no option was exercised by the taxpayer but he uses the amount deposited in capital gains account scheme to buy two residential houses, whether exemption will be denied to him in respect of one house;

(b) Having bought two houses, if the taxpayer sells one of the houses within 3 years, whether entire exemption will be withdrawn or only with reference to house sold. It is not clear can such taxpayer exercise option in future year.

(c) It may also be clarified that what is the exact time of exercise of option.

Such difficulties may be addressed either by way of legislative amendment and/or through a circular.

8.3.3 Provide Capital Gain Exemption on Buy Back of Rupee Denominated Bonds (RDBs)

Issue

- Any transfer, made outside India, of a capital asset being Rupee Denominated Bond (RDB) of an Indian company issued outside India, by a non-resident to another nonresident is exempt under section 47(viiaa) of the Act. But no exemption is provided for buyback of RDBs by Indian companies from non-resident investors. The terms of the issue of such bonds generally permit the Indian issuing company to buy them back, if so permitted by RBI. It may be recollected that RBI had permitted Indian companies in past to buy back FCCBs which were trading at discount in overseas stock exchange. The buyback at discount benefits the Indian economy by reducing the outflow of foreign exchange (For example, if bond with face value of $ 100 is bought back at $ 75, it results in foreign exchange savings of $ 25 for India). But the exemption is restricted to transfer from one non-resident to another non-resident. It does not cover transfer by

nonresident to Indian issuing company. Since the transaction takes in case of listed bonds through stock exchange mechanism, the non-resident seller will be unable to ascertain whether purchaser on the other side is non-resident or Indian issuing company. This creates ambiguity and practical challenge for non-resident sellers.

Recommendation

- It is suggested that the capital gains exemption under section 47(viiaa) of the Act be expanded to cover transfer of bonds from non-resident to Indian issuing company as a part of buyback.

8.3.4 Characterisation of Income from Transfer of Unlisted Shares

With a view to having a consistent view in assessments pertaining to income from transfer of unlisted shares, the CBDT has clarified that the income arising from transfer of unlisted shares would be considered under the head 'Capital Gain', irrespective of period of holding, with a view to avoid disputes/litigation and to maintain uniform approach.

However, this letter provides that this principle would not necessarily apply in situations where the transfer of unlisted shares is made along with the control and management of underlying business. It is provided that the Assessing Officer would take appropriate view in such situations. This leads to significant uncertainty as the change to the control and management is a direct result of the transfer of shares, and is often referred to in share purchase agreements to avoid contractual disputes and to ensure continuity of business. This should ideally have no bearing on the characterisation of income from sale of shares.

Given the above, our recommendations are as under:-

- Transfer of control and management has no direct bearing on the characterisation of income from the transfer of shares. It is therefore necessary to address this anomaly and it should be provided that even in cases where transfer of shares results in transfer of control and management of underlying business, gains arising therefrom should be assessed under the head ‘Capital Gains’.
- Also, it is pertinent to note that the definition of “capital asset” specifically includes management and control rights qua an Indian company. Accordingly, the purpose of this carve out is unclear as no basis is given for such an exclusion and could lead to unnecessary litigation.
- Further, the current Circular deals only with sale of unlisted shares and the same should be extended to all unlisted securities such as debentures and bonds of public and private limited companies.
- Also, similar to earlier Circular dated 29 February 2016 which was issued in the context of listed securities, an option should be provided to the assessee to treat the income as business income in case where shares of unlisted companies are held as stock in trade on a consistent basis.

8.3.5 Extension of capital gain exemption to Foreign Currency Denominated Bonds

Issues

Indian corporates have been raising funds from a source outside India by way Foreign Currency Denominated Bonds (FCDB) through External Commercial Borrowing. There is no specific exemption on transfer of FCDB from non-resident to non-resident outside India.

Nature of Foreign Currency Denominated Bonds are similar to that of Rupee Denominated

Bonds (RDB)/Masala Bond. RDB are given specific exemption under section 47(viiaa) of the Act wherein, any transfer of capital asset, being RDB of Indian company issued outside India, by a non- resident to another non- resident shall not be regarded as transfer.

On similar lines, transfer exemption between non-residents to another non-resident should be extended to FCDB also.

Further, transfer of bonds, being Global depositary receipts, by one non-resident to another non-residents are also not considered as transfer under section 47(viia) of the Act.

Recommendation

Transfer exemption between non-residents to another non-resident should also be extended to non-resident investor investing in FCDB.

8.3.6 Step down subsidiaries where the parent company holds whole of share capital of such subsidiary directly or through other 100% held subsidiary be exempt under Section 47

Issues

- Under the existing provisions of clause (iv) and (v) of Section 47 of the Act, transfer of a capital asset by a holding company to its subsidiary company and vice versa is not regarded as a 'transfer' for the purposes of capital gains if inter-alia, the parent company holds whole of the share capital of subsidiary company.
- In order to carry out business in today's challenging business environment, business houses create multilayer corporate structure for complying with various regulatory and contractual requirements as well as risk ring fencing for its lenders.

Recommendation

- It is therefore, suggested that benefits of clause (iv) and (v) of Section 47 may be extended to step down subsidiaries where the parent company holds whole of share capital of such subsidiary directly or through other 100% held subsidiary.

8.3.7 Consequential cost step up for depreciation on trigger of claw back provision of section 47A in case of transfer of capital asset by holding/subsidiary company

(a) As a logical consequence of withdrawal of capital gains exemption in hands of transferor on trigger of section 47A and similar to section 49(3) for non-depreciable assets, it should be provided in section 43(1) and section 43(6) that the 'actual cost' and 'written

down value' of depreciable asset in hands of the transferee will stand recomputed as per actual cost incurred by the transferee.

(b) While section 155(7B) of the Act provides for extended time limit of 4 years from the year of trigger of section 47A to re-compute total income of transferor, provisions of section 155(7B) of the Act may be amended to provide extended time limit to recompute total income of transferee as well (i.e. to recompute depreciation allowance from the year of acquisition).

8.3.8 Conversion into Limited Liability Partnership/Conversion of Firm into Company

Issues

- Section 47(xiiib) of the Act provides tax neutrality to conversion of Company into LLP subject to certain stringent conditions. LLP as a form of business organization is extremely important. The mid-size and smaller businesses are finding it extremely difficult to comply with very heavy compliance requirements under the Companies Act, and of course, they are aware that this will prevent them from accessing the capital market. However, conditions for conversion of a company into LLP should be made less stringent or some relaxation should be provided in application of the same as discussed below:- o Tax neutrality is available only to a Company having Turnover of less than Rs. 60 lakhs for 3 years prior to such conversion. In the current economic scenario, this limit of Rs. 60 lakhs needs to be removed. There is no reason, why companies with large turnover, which otherwise qualify, should not be eligible for conversion with tax neutrality.
    - Another condition is that all the shareholders of the company, immediately before the conversion, should become partners of the LLP. This condition should be made applicable only in respect of equity shareholders and not preference shareholders, since preference shares are in the nature of quasi equity.
    - Further, it is necessary that the aggregate of the profit sharing ratio of the shareholders of the company, in the LLP shall not be less than 50% at any time during the period of five years from the date of conversion. This condition should be applicable only to voluntary transfers and not to all the transfers. Say, this condition should not apply in case of dilution resulting from death or disqualification of a partner or amalgamation of a corporate partner.
    - For claiming tax neutrality, it is provided that accumulated profits of the company as on the date of conversion should not be paid to the partners of the LLP for a period of three years from date of conversion. Under the Act, LLP is considered akin to a partnership firm and there is no restriction on distribution of the profits of the partnership firm. Further in case of firm, there is no requirement to show reserves and surplus separately, but the same is credited to partner's capital account. Thus, there should not be any restriction on LLP in relation to payment out of profits.

      Further, the term accumulated profits is not defined and may include other reserves also.

- MAT payment under Section 115JB of the Act is prepayment of taxes actually becoming due in subsequent years under normal provisions of the Act. Consequently, Section 115JAA of the Act allows credit for such payments in the year the company becomes liable to pay tax under normal provisions of the Act. There is no reason, why such credit should not be allowed to LLP, which is converted from a company eligible to such credits, if it is paying taxes under normal provisions of the Act.
- Section 47(xiii)/(xiiib) and (xiv) of the Act requires that the members of the firm/ shareholders of the company should continue to maintain profit sharing/ shareholding for 5 years. It should be noted that 5 years is a fairly long time and therefore, it should be restricted to 3 years.
- Section 47A(4) of the Act provides that in case of non-compliance of any condition provided in Section 47(xiiib) of the Act, the gains on conversion of company/ transfer of shares shall be the profits & gains taxable in the hands of the LLP/ shareholders in the year of such non-compliance. Similarly, proviso to Section 72A(6A) of the Act provides that in case of non-compliance of any condition provided in section 47(xiiib) of the Act, the losses/unabsorbed depreciation of the company utilized by the LLP shall be income of the LLP for the year of such non-compliance.
- Section 47A(3) of the Act provides that in case of non-compliance of any condition provided in Section 47(xiii) or (xiv) of the Act, the gains on conversion of partnership or proprietary concern shall be profits & gains taxable in the hands of the Company in the year of such non-compliance. Similar to Section 72A(6A), 72A(6) deals with cases covered under Section 47(xiii) and (xiv).

- The conversion of a company into LLP will become all the more difficult now as a result of amendment made in section 47(xiiib) of the Act by the Finance Act 2016 which denies exemption in a case where the company was possessed of total assets worth Rs. 5 crores in any of the 3 prior years. Also, the expression "total value of the assets as appearing in the books of accounts" is not defined and may create certain interpretational issues such as whether status of assets is to be seen on balance sheet date or even one day's presence during the year will be considered even if asset no longer exists with the assessee as on balance sheet date. Also, whether 'Miscellaneous Expense' and Advance tax (with corresponding provisions for tax on liability side), etc. reflected on asset side of balance sheet will constitute an asset, are the other issues which need to be addressed.
- Section 47(xiiib) of the Act provides tax neutrality to conversion of Company into LLP. Further, section 72A of the Act provides for carry forward of losses in case of merger/demerger of two companies. There is no enabling provision for tax neutral conversion of partnership firm into LLP or merger of two LLPs. Also, there is no enabling provision under the Act for carry forward of losses in case of merger/demerger of two LLPs.

Recommendations

- Turnover criteria should be removed from Section 47(xiiib) of the Act.

- Words “equity shareholder” should substitute the word “shareholder” wherever it appears in Section 47(xiiib) of the Act.
- Insert proviso under clause (d) in proviso to Section 47(xiiib) of the Act to provide that it should not be applicable to a case where a change in profit sharing takes place consequent to death of a partner or pursuant to any other transaction covered under Section 47 of the Act.
- Condition of non-payment out of accumulated profits specified in clause (f) to proviso to Section 47(xiiib) of the Act should be removed. If not removed, term accumulated profit should be appropriately defined.
- Provisions of Section 115JAA of the Act allowing utilization of MAT credit should be amended to allowed credit for MAT paid by the company to the successor LLP.
- Sections 47(xiii)/(xiiib)/(xiv) should be amended to reduce period of continuing same profit sharing/shareholding from 5 years to 3 years.
- Words profits & gains in Section 47A(3)/(4) of the Act should be replaced with the income.
- In view of making conversion of a company into a LLP more liberal, it is recommended that the condition of asset base being less than Rs. 5 crores be rationalised. Further, the scope of the term ‘total value of the assets as appearing in the books of accounts’ be clarified to provide certainty and reduce litigation.
- It is suggested that suitable provisions be introduced in the Act to allow tax neutral conversion of partnership firm into LLP or merger of two LLPs. It is further recommended that the benefit of section 72A of the Act be extended to merger and demerger undertaken between LLPs.

8.3.9 Provide Tax Neutrality in case of Overseas Reorganization - Requirement of transferee company to be an Indian Company under Section 47(vi) and (vii) of the Act should be removed

Issues

- The provisions of the Act are framed to provide tax neutrality only in cases where the amalgamated company is an Indian company. Section 47(vii) of the Act provides that a transfer of shares by the shareholder of an amalgamating company would not be liable to capital gains tax subject to the following conditions:- o The transfer is made in consideration of the allotment to him of any share or shares in the amalgamated company, and
- The amalgamated company is an Indian company.
- Clearly, the above exemption would be allowed only in case a foreign company is merged into an Indian company and not vice-versa. In other words, if an Indian company merges into a foreign company and the payment of consideration to the shareholders of the merging company is in cash, or in Depository Receipts, or partly in cash and partly in

Depository Receipts, as envisaged in Section 234 of the Companies Act, 2013, the amalgamating company and its shareholders would be subject to capital gains tax in India.

- In the emerging global scenario it is important that the merger of Indian companies into foreign companies should be legally recognised and made pari-passu with the merger of foreign companies into Indian companies, particularly for income tax purposes.

Recommendations

- It is suggested that the requirement of transferee company to be an Indian Company under Section 47(vi) and (vii) of the Act should be removed.
- It is further recommended that appropriate provisions be introduced in the Act to allow carry forward of losses in case of merger of an Indian company with foreign company.

8.3.10 Reduce holding period for REIT/Invit units to one year to turn long term to align with holding period for equity instruments

Issue

- Business trusts like REITs and InvITs have gained increasing popularity as a means of investment in assets in the infrastructure sector. Recognizing the same, the Government has also provided pass-through status for investments made through business trusts.
- However, investment in units of REITs and InvITs will turn long term only on holding the investment for a minimum of 36 months as against a period of 12 months prescribed for investment in listed securities. Such long period disincentivizes investors from seriously considering investment through business trusts given the higher tax rate attracted when the gains are short term in nature.
- REITS and InvITS are envisaged to play major role in success of Government’s National Monetisation Pipeline of Rs. 6 lakh crores. To increase the attractiveness of such investment for both foreign and domestic investors, it should have same treatment as listed equity instruments.

Recommendation

- It is recommended to bring down the period of holding for units in REITs and InvITs to be classified as long term to 12 months at par with listed securities.

8.4 Transfer Pricing

8.4.1 Limitation of Interest Benefit – Section 94B

The Finance Act, 2017 has introduced section 94B in the Act relating to limitation of interest benefit (deduction). Where an Indian company, or a permanent establishment of a foreign company in India, being the borrower, pays interest exceeding Rs. one crore in respect of any debt issued/ guaranteed (implicitly or explicitly) by a non-resident AE, then the interest shall not be deductible in computing income chargeable under the head ‘Profits and gains of business or profession’ to the extent, it qualifies as excess interest.

Excess interest shall mean total interest paid/payable by the taxpayer in excess of thirty per cent of cash profits or earnings before interest, taxes, depreciation and amortization; or interest paid or payable to AEs for that previous year, whichever is less.

There will be restriction on the deductibility of the interest in the hands of the taxpayer in a particular financial year to the extent it is excess, as explained above. However, the same shall be allowed to be carried forward for a period of eight years and allowed as deduction in subsequent years. The above restrictions shall not be applicable to taxpayers engaged in the business of banking or insurance. These provisions are applicable for AY 2018-19 and subsequent years.

Issues

- India is a developing country with a need for foreign investment to fund various initiatives, in particular the development of infrastructure. However, the restrictions imposed under section 94B of the Act in respect of interest of overseas loans is creating uncertainty for foreign as well as Indian parties at a policy level on overseas borrowing.
- The rate of interest in India is high as compared to other developed nations. Certain business requires huge funding in the initial period of operations especially start-ups. Given the same, the threshold of Rs. 1 crore is low and should be increased. The threshold of interest expenditure for applicability of this section should be increased to at least Rs. 15 crores.
- Interest limitation rules are in nascent stage, companies must be provided transition window to re-align its debt structure. Further, aligning the capital structure is time consuming and requires regulatory approvals. It is recommended that the Earnings before interest, taxes, depreciation and amortisation (‘EBITDA’) capping should be initially @ 60-70% and phased reduction of the same to 30% could be provided over a span of three years.
- NBFCs have interest income as main source of income and huge corresponding interest expenses. So capping deduction of interest on such companies will lead to harsh consequences for NBFC’s. Interest limitation rules do not apply to an Indian Company/ PE of Foreign company which is engaged in the business of banking or insurance. Like banking or insurance business, an exclusion of NBFC Companies from interest limitation rules is suggested.
- As per the term ‘debt’ provided in clause (ii) of sub-section 5 of section 94B, interest may include many other payments made on various kinds of financial arrangements and instruments. Further, there is lack of clarity on the mechanism to calculate EBITDA i.e. book profit calculated on the basis of accounting standards, Ind-AS or otherwise or as per the provisions of the Act. This may result in unnecessary litigation. The BEPS Action Plan 4 provides for a Group Ratio Rule wherein the Group’s overall third party interest as a proportion of the Group’s EBITDA is computed and that ratio is applied to the individual company’s EBITDA to determine the interest restriction. This would take into account the actual third party debt and leverage at global level vis-à-vis third parties.

- Sub-section 4 to section 94B indicates “Where for any assessment year, the interest expenditure is not wholly deducted against income under the head "Profits and gains of business or profession", so much of the interest expenditure as has not been so deducted, shall be carried forward to the following assessment year or assessment years, and it shall be allowed as a deduction against the profits and gains, if any, of any business or profession carried on by it and assessable for that assessment year to the extent of maximum allowable interest expenditure in accordance with sub-section (2)”. There could be a situation that in any of the subsequent years, the proposed section becomes inapplicable to the assessee in case the interest expense is less than Rs. 1 crore. It is suggested that a clarification be provided that set off would be available even if section is not triggered in such subsequent year.
- Section 94B is introduced by Finance Act 2017 w.e.f. 1-4-2018. It is not clear as to whether the provision is applicable for existing debts or only for new debts taken on/or after 1 April 2017.
- Sub-section (2) to section 94B of the Act defines ‘excess interest’ to mean an amount of total interest paid or payable in excess of thirty per cent of EBITDA of the borrower in the previous year or interest paid or payable to associated enterprises for that previous year, whichever is less. In case of domestic as well as foreign borrowings, for the purpose of interest disallowance, domestic interest would also be considered due to reading of ‘total interest’. If that be the case, it would result into higher disallowance of foreign interest as compared to normal scenario where there is no domestic borrowings.
- Second proviso to section 94B of the Act provides “Provided that no interest expenditure shall be carried forward under this sub-section for more than eight assessment years immediately succeeding the assessment year for which the excess interest expenditure was first computed.” The interest disallowed is allowed to be set off in subsequent years for a period of 8 years. If the company is subject to tax under MAT, it would not be able to set it off within 8 years.
- Section 94B of the Act provides for disallowance of interest in certain situation. Additionally, disallowance can also trigger under section 40(1) (i) and 43B of the Act. There could be a situation that the interest may also be disallowed under section 40(a)(i) for non-deduction of taxes and/or under section 43B of the Act for non-payment of interest before the due date of filing the return of income. Clarification should be provided that interest so disallowed under section 40(a)(i) or 43B be specifically excluded from definition of “total interest”.

Recommendations

- In view of the policy level issues on overseas borrowings, the restrictions imposed on the interest benefits on overseas borrowings should be done away with entirely or at least deferred for 5-10 years to give India a chance to achieve its anticipated growth through required infrastructural development and maturity.
- The de minimis threshold should be increased to Rs. 15 crores.

- It is suggested that EBITDA capping should be initially @ 60-70% and phased reduction of the same to 30% could be provided over a span of three years.
- Where assessee is having interest income, net interest expenditure must be considered for the purpose of determining applicability of section 94B of the Act.
- It is suggested that the section should be made applicable to new debts taken on or after 1 April 2017.
- It is suggested that interest should be restricted only to foreign AE interest and not total interest. Irrespective of domestic borrowings, only foreign AE interest in excess of 30% of EBDITA should be disallowed.
- It is recommended that there should not be any restrictions on number of years for carry forward of unutilised interest like depreciation claim.
- The exclusions granted to banking and insurance companies should also be extended to other sectors such as Non-Banking Finance Companies, large capital intensive companies with long gestation periods and companies in the real estate sector and the infrastructure sector (requiring significant foreign capital which may not always come in the form of equity).
- The section should be amended to specify that in guarantee cases limitation would apply only to the extent of the guarantee commission (if any) paid by the Indian entity to the overseas guarantor (being its AE) and not on the interest paid to the third party lender.
- Appropriate guidelines may be issued to clarify what the term 'interest or of similar nature' should include or exclude as the definition provided in the existing section 2(28A) may not be adequate for the purposes of section 94B based on the definition of the term 'debt'.
- Further, the word 'implicit guarantee' should be dropped from the provisions. The term 'explicit guarantee' should also be appropriately defined to obviate future litigation on this front.
- The mechanism to calculate EBITDA should be clearly laid down. EBITDA should exclude non-taxable/exempt income/foreign dividend taxable under section 115BBD of the Act and interest towards earning of non-taxable/exempt income/foreign dividend taxable under section 115BBD of the Act should also excluded.
- In lieu of a fixed 30% EBITDA restriction, a Group Ratio could be considered in order to apply the interest deduction restriction under this provision. The Group Ratio refers to the Group's overall third party interest as a proportion of the Group's EBITDA and that ratio is applied to the individual company's EBITDA to determine the interest restriction. This would take into account the actual third party debt and leverage at global level visà-vis third parties.
- Similar to provision of section 72A of the Act, carried forward interest expenditure should be allowed for set off in hands of transferee company in case of business organisation such as amalgamation, demerger or slump sale. Appropriate provisions be

introduced in the Act to provide that the amount of unabsorbed interest amount shall be available for carry forward to the successor entity in case of business reorganization.

- The section is open to interpretation on the applicability of the section in case the company incurs the losses. It is submitted that a suitable clarification is required on this issue.

8.4.2 Range to be broadened to 25%-75% - interquartile (IQR)

CBDT has notified the final rules for using the range concept and multiple year data in determination of Arm's Length Price. As per the rules prescribed by the Government for application of range, the margins in the data set (i.e., set of comparable companies) are required to be arranged in ascending order and the arm's length range would be data points lying between the 35th and 65th percentile of the data set.

Recommendation

The 35th to 65th range is a very narrow range. It is very unique and is normally not followed globally. In most cases, the arithmetic mean does not fall within this range. In fact in most cases, the mean falls within the inter quartile range. Thus, it is recommended that an inter quartile range i.e. data points lying between 25th to 75th percentile should be prescribed as it is an internationally accepted norm. This would go a long way in reducing litigation.

8.4.3 Introduce term test concept for benchmarking the consolidated margins earned by the tested party

Issue

In certain business segments where long term project is a norm (construction, power generation, Oil and gas, etc.), companies enter into long term contracts (spanning for a period of 2-5 years), the pricing is determined considering the market competitiveness and overall margins that can be earned on the entire project (also factoring the subsequent maintenance related business in such project). However, year by year margins on the project fluctuate basis the completion of the project and scope of work completed.

Recommendation

Considering the tax principle that every year is a separate year for tax assessment, the current TP regulations provide for benchmarking the margins of a legal entity year on year basis without factoring the overall margins of the entity over a period of time. This results in having TP adjustments in one year due to lower margins without any corresponding reversal in subsequent years when the margins exceed the arm's length margins. Considering this business scenario in mind, concept of term test for benchmarking the margins over a range of years can be introduced in the Act in line with the OECD guidelines.

8.4.4 Block assessment to be considered for some issues

Under the current transfer pricing regime, assessment is carried out separately for each assessment year irrespective of the nature of the issue.

Recommendation

It is suggested that block assessment of 3-5 years should be considered for issues like royalties and other principle issues, as they are cyclical in nature and carrying out a separate assessment for every year result in wastage of time and resources of the taxpayer and the tax department. A mechanism for detailed assessment in the first year of the prescribed block which should be made applicable for the remaining years of the block be evolved. This would help us to align our practices with global best practices. Such block assessment will free up administrative resources for the revenue also and will also reduce the litigation burden of the taxpayer.

8.4.5 Detailed guidelines on issues like location Savings, Marketing Intangibles, Cost contribution arrangements, Intra-group services, benchmarking of loans and guarantees

A plethora of litigation on transfer pricing matters in India revolves around the following issues:-

- compensation for location savings,
- compensation for development of marketing intangibles and their economic ownership and related returns,
- compensation for other intangibles where significant functions related to development, enhancement, maintenance, protection and exploitation (DEMPE) are carried out in India,
- Cost contribution arrangements
- intra-group service charges,
- inbound and outbound loans and guarantees, etc.

There are no specific guiding principles currently in the Indian Transfer Pricing (TP) regulations to determine arm's length compensation for the above transactions/ situations (except for receipt of low value intra group services, introduced recently under the revised safe harbour rules).

As regards marketing intangibles there are some important rulings where the Tribunals and Courts have laid down certain important principles, but these rulings do not provide clear guidance on what methodologies/approaches can be adopted by the taxpayers for determining arm's length price. There are also several contradicting judgments on these matters.

Recommendation

In the absence of any guidance or industry benchmarks in public domain for testing such transactions, it is suggested that detailed guidelines in line with the Organisation of Economic Co-operation and Development (OECD) Base Erosion Profit Shifting (BEPS) Action Plans 8-10, where India has also provided its consensus need to be introduced in the Indian transfer pricing regulations.

8.4.6 Roll Back of Advance Pricing Agreement (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. In this regard, some of the aspects that need to be further addressed are as under.

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

- This provision should be relaxed to the extent that taxpayers with similar transactions with no substantial changes in 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. Thus, this provision should be made applicable to similar nature of transactions and with different AEs.
- 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.

8.4.7 Allocate more resources to Advance Pricing Agreement (APA) program to clear existing backlog and new cases arising due to Covid related impact

Issue

- The Advance Pricing Agreement (APA) mechanism for settlement of TP disputes was introduced in 2012 with the objective of providing much needed tax certainty to MNEs operating in India with regard to their intra-group transactions.
- While the program has attained success invoking significant interest with over 1000 applications being filed and over 300 APAs being signed, at the same time, it has also faced certain challenges such as augmentation of resources (which are also acknowledged by the CBDT).
- APAs play a significant role in enhancing ease of doing business and avoiding tax litigation. Accordingly, there is an acute need to enlarge the benefits of the program, as well as to cope with the increased burden resulting out of the COVID-19 pandemic which has caused much uncertainty on business models.

Recommendation

- At the outset, augmentation of the APA teams with appropriate number of officers having the appropriate skills, knowledge and subject matter expertise may be

imperative to bring down the pendency of cases along with providing a stability of tenure to such personnel.

- A review may be conducted of the entire lifecycle of APA process and the process may be streamlined to improve on timelines by reducing delays by use of technology. For instance, video calls may be held instead of physical meetings.

8.4.8 Rationalise Safe Harbour Rules

Issues and Recommendations

Provide corporate guarantee – with safe harbour rate being not less than 1% per annum on the amount guaranteed

a) Rationalisation of safe harbour rate of guarantee commission

It would not be irrational to imagine that the banks and financial institutions may sturdily insist on explicit guarantee, in view of COVID-19 driven financial turmoil, while entering into new financing arrangements/renewing the existing financing arrangements. Hence, a sudden rise in such explicit guarantee transactions between group companies of MNCs may be witnessed. This would also give rise to expectations of various stakeholders that existing safe harbour rate of guarantee commission be rationalised by aligning it with the new economic realities shaped by the COVID-19 pandemic.

The quantum of guarantee commission/fee should not outweigh the benefit conferred by the guarantee in the form of reduced interest cost. In current prevailing economic circumstances, existing safe harbour guarantee commission rate of minimum 1% may not justify the benefit in the form of interest differential. Moreover, tax judicial authorities in India have also, in many cases, held guaranteed commission of 0.5% to be at arm's length. Hence, it is highly recommended that the CBDT may consider lowering the minimum guarantee commission rate appropriately by giving due weight to the current economic scenario.

b) Widening the scope of eligible international transaction

There is an indispensable need to bring transactions of availing of loan within the purview of safe harbour rules on account of prevailing economic conditions, it is highly recommended that international transactions of receipt of corporate guarantee are also considered by the CBDT as eligible international transaction. This is also a need of the hour as there would be resurgence of loan and guarantee arrangements between group companies due to the impact of COVID-19 on the financial stability and liquidity in the global markets. Further, it is also recommended that the scope of existing eligible international transaction providing of corporate guarantee is expanded to cover such international transactions with other associated enterprises who may not be wholly owned subsidiary.

c) Guarantee commission

Moratorium where Associated Entity is incurring losses due to COVID-19 pandemic. CBDT should consider allowing moratorium from charging of guarantee fee on the amounts guaranteed for Financial Year (FY) 2020-21 where the Indian company is opting for safe

harbour for a block of 3 years starting from FY 2020-21 and if the overseas AE has incurred losses due to COVID-19.

Manufacture and export of core auto components – with safe harbour rate being not less than 12% on operating cost

Manufacture and export of non-core auto components – with safe harbour rate being not less than 8.5% on operating cost

a) Rationalisation of safe harbour margins

Automotive industry is experiencing hardest hit due to unending the COVID-19 pandemic. Adverse impact on the Indian auto components industry, of global slowdown in automotive industry and regulatory measures in the form of shift from BS IV to BS VI standard, has been further fuelled by COVID-19 situation. Hence, the industry has fairly high expectations that the CBDT streamline the safe harbour margins, which reasonably reflect the current economic and industry realities in this challenging time. The CBDT may consider applying the similar approach as discussed for the provision of service transaction earlier wherein the benefits in terms of margin reduction is provided in the initial years of the block.

Moreover, the CBDT may also consider stimulating auto components industry players, which caters to electric vehicles (EV) by proposing lower safe harbour rates. Such move by the CBDT will also be in line with the Indian government's policy of promoting EV vertical in the country and it would also contribute to the creation of employment opportunities in India.

b) Widening the scope of SH coverage

In order to promote the domestic manufacturing, the GOI has introduced Production Linked Incentive (PLI) scheme for 10 key sectors i.e., electronics and technology, pharmaceutical, telecom and networking equipments, textile products, food products, steel products, advance chemistry cell battery, automobile and auto components, etc.

Therefore, CBDT should consider extending the SH rates for companies engaged in manufacturing and covered under PLI scheme of GOI and propose the SH margin of 10% on Operating cost in year one and two and further lower it for subsequent years when the turnover of the Indian company increases. The turnover threshold for this benefit could be the revised MSME threshold.

8.4.9 Valuation under Customs and Transfer Pricing

Both Customs and TP require taxpayer to establish arm's length principle with respect to transactions between related parties. Objective under respective laws is to provide safeguard measures to ensure that taxable values (whether it is import value of goods or reported tax profits) are the correct values on which respective taxes are levied. The above objective, while established on a common platform has diverse end-results as seen below:

- To increase Customs duty amounts, the Customs (GATT Valuation) Cell would prefer to increase the import value of goods.
- To increase tax, the Revenue Authorities would prefer to reduce purchase price of goods.

Issues

- The diverse end-results create ambiguity in the manner in which the taxpayer should report values under the Customs and the Transfer Pricing. There are various contradicting judicial precedents which favour and contradict the use of custom valuation in transfer pricing.
- These contradicting decisions necessitate a greater need for convergence of transfer pricing mechanism under the Act and the Customs Regulations.

Recommendation

- There is a need for a common platform that would provide a 'middle-path' of arm’s length price that is equally acceptable under Customs Law and under the Transfer Pricing.

8.4.10 Filing of Form 3CEB by Foreign Companies - Provisions of Indian transfer pricing would not apply to foreign companies/foreign residents unless they have a permanent establishment in India

Issue

The foreign companies are required to file Transfer Pricing report in Form 3CEB in India, even if income subject to an international transaction is not chargeable to tax in India or where the transaction entered with the foreign entity is already reported by the Indian entity in its Form 3CEB as per the provisions of the existing Indian transfer pricing law. It may be noted that, in principle, the foreign residents not having a permanent establishment in India should not be required to file Transfer Pricing report (Form 3CEB) in India keeping in view the compliances done by the Indian entity.

Recommendation

It is suggested that the Government should clear the ambiguity surrounding this issue by clarifying that the provisions of Indian transfer pricing would not apply to foreign companies/foreign residents unless they have a permanent establishment in India.

8.5 Tax Deducted at Source (TDS)

8.5.1 Clarify applicability of treaty benefit while deducting tax on payments to non-residents under provisions which provide for specific rate of TDS (as distinguished from ‘rates in force’ under section 195)

Issues

- The Hon’ble Supreme Court in a recent decision in the case of PILCOM v. CIT (2020)(116 taxmann.com 394) held that the payer cannot consider DTAA benefit available to the non-resident payee at the stage of TDS on payments to such non-resident payees, in a case where the transaction was not covered by section 195 of the Act.
- The SC was concerned with a case where PILCOM made payments in nature of guarantee money to non-resident sports association related to the cricket matches played in India, Sri Lanka and Pakistan during Cricket World Cup 1996. The SC held that

once it is established that the payments made to the non-resident sports associations were 'in relation to' to the matches played in India, such guarantee money can be said to be earned from a source in India and hence, the income is deemed to accrue or arise in India attracting corresponding withholding obligation for the payer. The Honourable SC has taken a view that, in a case where the TDS rate is provided in a specific section, the DTAA rate of tax may not be taken into account.

- Prior to the pronouncement of the judgment, it was considered fairly well settled that the tax withholding can be made at DTAA rate in a case where it was lower than rate provided in the ITA or relevant Finance Act. The Tax Authorities as also taxpayers have complied with TDS compliances on such understanding. This approach was also perceived to be in sync with earlier judgments of SC in the cases of CIT v. Eli Lilly and Co. (India) Pvt. Ltd. [2009] (312 ITR 225), G.E. India Technology Centre Pvt. Ltd. v. CIT [2010] (327 ITR 456) and Vijay Ship Breaking Corporation v CIT [2009] (314 ITR 309).
- Section 195(2) and section 197 of the Act permit the taxpayers to apply for nil or lower rate of tax if DTAA rate is lower than the rates specified in the domestic law. The tax policy behind these provisions is inter alia, guided by the ease of operation without injuring interests of Revenue. There may not be insistence on collection of tax which is higher than the amount of primary tax liability incurred by the NR taxpayer having regard to DTAA provisions.
- As a fall out of SC judgment in PILCOM's case, many apprehensions have arisen in the minds of the taxpayers on the exact scope, applicability and width of the ratio of the judgment. There is also an apprehension on the extent to which the earlier judgments of the SC may be regarded as inapplicable or distinguishable. Doubts have also arisen about the posture that CBDT may adopt with regard to the ongoing /future and the past transactions.

Amongst others, the following apprehensions are raised by taxpayers:-

a) Whether the ratio of PILCOM ruling will be restricted to a case covered by section 194E or will it apply to all other provisions of ITA where specific TDS rate is specified within the section?

b) Whether the ratio of PILCOM ruling be considered by CBDT to be applicable also in a case where the tax payable by income recipient is nil either as a result of DTAA or as a result of section 10 or other exemption provisions of the Act or as a result of certain other international agreements under which exemption may have been conceded by India.

c) Do the earlier judgments of SC continue to hold the field, and if yes, the extent to which CBDT will consider various judgments to be reconcilable in terms of compliance by the taxpayer.

d) Will PILCOM judgment have prospective implication in terms of compliance expectation from the tax deductors?

e) Whether Tax Department will reopen past cases based on this ruling to recover shortfall of TDS being the difference between TDS rate as per Act and tax rate as per treaty to raise demands along with interest under section 201(1A)?

f) Whether Tax Department will also levy penalty under section 271C or initiate prosecution under section 276B?

g) Going forward, whether non-residents will suffer higher TDS due to application of ratio of PILCOM ruling and will necessarily be required to file return to claim refund of excess TDS?

h) Will CBDT consider appropriate Circular to be issued under S. 119 and/or notification under S.197(1F) of ITA to permit the taxpayers, under the shelter of administrative dispension, to follow the same course of action as was being followed prior to PILCOM ruling?

Rationale:

i) As a matter of tax policy, India has, till date avoided the policy of 'retain and refund', and has consistently adopted a tax policy where TDS is restricted to the amount of the actual tax liability incurred by the NR recipient of income. This has eased compliance on the taxpayers as also administrative burden for the Tax Department.

j) Such tax policy, if continued to be applied, may harmonize with the thinking that TDS is secondary tax obligation and should ideally follow the primary tax obligation.

k) In order to avoid any form of differentiation or discrimination, the tax policy may adopt procedure which, on principles, treats all the taxpayers at par.

l) Finance Act 2021 amended s.196D relevant to TDS on payments to FPIs to provide for application of treaty rates for TDS purposes. This was specifically in view of PILCOM ratio. Similar amendments are required for other provisions which provide for fixed rate of TDS on payments to non-residents.

Recommendations

m) Without prejudice to our other submissions, it is submitted that the CBDT may clarify the following and/or adopt appropriate legislative process to so as to avoid hardship to the taxpayers and to ease the burden of compliance:-

   - It may be clarified that the ratio of SC ruling in PILCOM's case applies only to those TDS provisions which provide for specific TDS rate and would not apply in determination of TDS liability under S.195 and other provisions which require TDS at 'rates in force'.
   - It may be clarified that any payment made to a non-resident, except in a case which is specifically excluded under S. 195 of ITA, may be considered as covered by S. 195 of ITA concurrently with any other provision of the Act so that treaty benefit can be considered by the payer for TDS purposes.

- Even in respect of payments which are specifically excluded from s.195 being interest covered by s.194LB, s.194LC and s.194LD, it may be clarified through a Circular and/or notification may be issued u/s. 197A(1F) that treaty benefit can be considered by the payer for TDS purposes.
- It may be clarified that the ratio of SC judgment in PILCOM's case will be considered to have prospective application in terms of the expectation of compliance obligation from the taxpayers and accordingly, no notices will be issued and/or demands will be raised for past years where payers have considered treaty benefits while making payments under TDS provisions requiring TDS at specific rates.

Without prejudice, in harmony with the tax policy adopted so far, and in exercise of the powers contained in S. 119 and/or S.197(1F), it may be clarified through a Circular/Notification (failing which, through suitable legislative amendment) that even where TDS is provided at specific rate for payment to non-resident (as distinguished from 'rates in force'), the payer can consider treaty benefit for TDS purposes.

8.5.2 Relax Onerous Form 15CA compliance in respect of dividend payment to Non-Resident

Issues

- As per Rule 37BB of the Rules, any person responsible for making any payment to a non-resident is required to furnish information in Form 15CA.
- As per the above provisions of the Act and IT Rules, any company responsible for paying dividend to a Non-Resident shareholder, is required to deduct tax at source and issue Form 15CA in respect of the said payment.
- Such Form is required to be uploaded on the income tax portal in respect of each & every non-resident shareholder and acknowledgment thereof is required to be shared with AD bank for remitting the money to the shareholders.
- For a large listed company which may have several Non-Resident Shareholders, this becomes a massive exercise as though the dividend remittance has to happen within 30 days from the date of declaration, the list of shareholders become available only on the record date and hence there is a very limited time available for the company to prepare these Forms and upload them on the income tax portal, in respect of each shareholder, even where the remittance does not even exceed Rs. 50,000/- for an individual shareholder. This adds to unnecessary compliance burden on the company.
- Since Form 15CA is merely a declaration of remitter and is used as a tool for collecting information in respect of payments which are chargeable to tax in the hands of recipient non-resident, as long as TDS has been deducted by the company at the time of payment of dividend to non-resident shareholder, the same level of information is anyways available with Income Tax authorities through TDS return filed by the company. Therefore, furnishing Form 15CA does not aid in collecting any additional information, except for increasing compliance for the company.

Recommendation

- The requirement to issue Form 15CA in respect of dividend payment to non-resident shareholder should be relaxed where the payment does not exceed Rs. 50,000/- This would significantly reduce the compliance burden for the company.
- Alternately, one single Form 15CA should be allowed to be uploaded for all non-resident shareholders with a suitable annexure, where PAN & other details of individual shareholders can be provided.

8.5.3 Provide relief from deduction of tax at source on payments that are accrued but are not due to the payee

Issues

- Most of the companies record provision entries towards various expenditures on a monthly basis to report performance to their parent entities. These entries are reversed in the subsequent month.
- These accruals are made on very broad estimates. The tax officers have been insisting that tax be deducted on these provisional entries.
- Year-end provisions are made by assessees to follow accrual system of accounting. Very often provision for expenses at the year-end are made based on best estimates available with the assessee even if the supporting invoice is received at the subsequent date. In most of the cases, even the identity of the payee is not known and a consolidated liability is provided on an entirely ad-hoc basis. Owing to such ad-hoc nature of such liabilities, they are mostly reversed at the start of the succeeding year and whenever identity of the payees and amounts payable to them becomes clear, liability for the same is provided subsequently.
- As per the current tax regime, tax is required to be deducted on such provisions which often leads to excess deduction and deposit of tax, disputes with the vendor and causes hardship to the assesses.

Recommendation

It is recommended that relief from deduction of tax at source should be given on payments that are accrued but are not due to the payee and for which the payees are not identifiable and represents only a provision made on a month end and year end basis on estimated basis for reporting purpose and are reversed subsequently.

8.5.4 Clarify Issues on TDS on cash withdrawals – Section 194N

(i) It should be clarified that in case of joint account holders, banks may issue TDS certificate to the first account holder and TDS credit may be given accordingly;

(ii) Section 196 of the Act specifies that no tax shall be deducted on sums payable to the "Government" on any income accruing/arising to it. Likewise newly introduced section 194N also carves out cash withdrawals by "Government" from TDS @ 2%. However, the term "Government" is not defined in the Act which often leads to friction between

entities claiming themselves to be 'Government' and banks. For effective, smooth and proper TDS compliance, it is recommended that CBDT should provide guidance on what constitutes "Government" and if possible, an exhaustive list of entities which fall under the category of 'Government' may be issued by way of a Circular.

8.5.5 TDS on payment in respect of life insurance policy – Section 194DA

(i) Under the erstwhile provisions prior to amendment by Finance (No.2) Act 2019, the life insurance companies were liable to deduct TDS @ 1% on the gross amount paid to the policy holders.

(ii) However, as per amended section 194DA post Finance (No.2) Act 2019, TDS is required to be made @ 5% on the 'income' component. Since TDS is an onerous obligation, the term "income" may be defined explicitly for the purposes of TDS liability under section 194DA of the Act as sum paid or payable to the policyholder as reduced by aggregate of premiums received till the date inclusive of service tax and GST (as explained in Explanatory Memorandum).

(iii) This is for the reason that computation of income in the hands of recipient policyholder is a debatable issue i.e. - whether income is taxable as capital gains (with indexation benefit) or as income from other sources. TDS being a provisional collection of tax, computation of 'income' for TDS purposes may be simplified.

8.5.6 TDS Credit

Section 203 of the Act requires the deductor of TDS to issue the TDS certificate to the deductee to the effect that tax has been deducted and specifying the amount so deducted. The deductor has to log in to the TDS CPC website and download the certificate of the deductee and then send such certificate to the deductee.

Issues and Recommendations

- Every quarter the deductor is required to login into the TDS Reconciliation Analysis and Correction Enabling System (TRACES) website and download TDS certificate for all the deductees and forward the same to each deductee. In case deductor is a big organisation which has deducted TDS for thousands of parties, it is required to send the TDS certificate through mail or post separately to each deductee. Issuing TDS certificate to thousands of parties every quarter poses challenges and also consumes lot of time which can otherwise be used for operations of the deductor. This sometimes leads to incomplete or non-compliance with issue of TDS certificates.

  It is also the deductee who suffers by way of denial of TDS credit in absence of TDS certificate and therefore it is a must for the deductee to continuously chase each deductor for issue of TDS certificate. It may be relevant to mention here that the AO's do not always give TDS credit, especially for years in the past, on basis of Form 26AS appearing in the system but require hard copies of the TDS certificates.

- Conjoint reading of the Section 199 of the Act and Rule 37BA of the Rules framed thereunder suggests that credit for the tax deduction should be given/granted on the basis of information relating to deduction furnished by the deductor (i.e. Form 26AS)

and the information in the return of income of the claimant. The requisite details in respect of the tax deducted at source are available in the Form 26AS. The taxpayer may furnish the information relating to tax deducted at source in the return of income based on the details available in Form 26AS leading to inference that both the information furnished by deductor and information in the return of income are as per Form 26AS.

CBDT Circulars on issuing of TDS certificate

The CBDT vide Circular No 3/2011 dated 13 May 2011 and Circular No 1/2012 dated 9 April 2012 has mandated for all deductors to issue Form 16A which is generated from TIN (Tax Information Network) website.

- Further the CBDT in para 3 of Circular No 3/2011 specifically mentioned as under:-

  > *"3.* The Department has already enabled the online viewing of Form No. 26AS by deductees which contains TDS details of the deductee based on the TDS statement (eTDS statement) filed electronically by the deductor. Ideally, there should not be any mismatch between the figures reported in TDS certificate in Form No. 16A issued by the deductor and figures contained in Form No.26AS which has been generated on the basis of e-TDS statement filed by the deductor. However, it has been found that in some cases the figures contained in Form No. 26AS are different from the figures reported in Form No.16A. The gaps in Form No. 26AS and TDS certificate in Form No. 16A arise mainly on account of wrong data entry by the deductor or non-filing of e-TDS statement by the deductor. As at present, the activity of issuance of Form No.16A is distinct and independent of filing of e-TDS statement, the chances of mismatch between TDS certificate in Form No.16A and Form No. 26AS cannot be completely ruled out. To overcome the challenge of mismatch a common link has now been created between the TDS certificate in Form No.16A and Form No. 26AS through a facility in the Tax Information Network website (TIN Website) which will enable a deductor to download TDS certificate in Form No.16A from the TIN Website based on the figures reported in e-TDS statement filed by him. As both Form No.16A and Form No.26AS will be generated on the basis of figures reported by the deductor in the e-TDS statement filed, the likelihood of mismatch between Form No.16A and Form No.26AS will be completely eliminated .

- CBDT Instruction No. 4/2012 [F. No. 225/34/2011-ITA.II] dated 25 May 2012 states that

  > "where the difference between the TDS claim and matching TDS amount reported in AS26 data does not exceed Rs Five thousands, the TDS claim may be accepted without verification. CBDT Instruction 1/2012 dated 2 February 2012 and Instruction 2/2011 dated 9 February 2011 provides similarly.

- CBDT Instruction No. 4/2014 [F. No. 225/151/2014/ITA.II] dated 7 April 2014 at para (5.2.a) reads "AO should verify whether TDS credits claimed by the taxpayer are available in the 26AS. If the credits are available in 26AS, a suitable rectification order......should be passed".

- CBDT 's Action Plan for the First Quarter of FY 2015-16 dated 24 March 2015 refers to ….(b) Giving credit for prepaid taxes, reflected in Form 26AS post processing….".

The above clearly demonstrates that there would not be any variation between TDS credit reflecting in the Form 26AS and TDS credit as per Form 16A. Further, in addition to these circulars, the CBDT in Central Actions plan of 2015 has also directed to give TDS credit on the basis of Form 26AS. Thus, reducing the relevance of Form 16A for the purpose of claiming TDS credit.

It is therefore suggested that TDS credit should be allowed purely on the basis of Form 26AS (irrespective of the fact whether the same has been claimed in the return or not) and the procedural requirement for issue or obtaining of TDS certificate in the Form 16A should be dispensed with. It must be ensured the tax officer grants TDS credit as per Form 26AS and do not insist for production of Form 16A.

Section 155(14) of the Act requires taxpayer to submit Form 16A within two years from the end of assessment year in case credit for TDS is not granted by AO for non-filing of TDS certificates with the return of income. In view of the above suggestion, sub-section (14) of section 155 of the Act should be deleted.

Further, section 203 of the Act which requires deductor to issue TDS certificates to the deductee should be amended to clarify that section 203 requires every person deducting tax to furnish certificate of tax deducted however such certificate is not necessary for claiming credit for tax deducted at source and the credit for tax deducted at source shall be granted in manner specified in Rule 37BA of the Rules.

However, an exception may be made in respect of TDS made on salary payments and TDS made in absence of PAN (either at higher rates as per s.206AA or based on TRC as per Rule 37BC). This is for the reason that most employees rely on Form 16 to fill up their income tax returns. Further, where PAN is not available, Form 26AS of the deductee cannot be populated. Hence, in these exceptional cases, the existing system of issuing TDS certificates may be continued.

Credit for TDS in the hands of a person other than deductee – Rule 37BA

As per Rule 37BA(2) of the Rules, where under any provisions of the Act, the whole or any part of the income on which tax has been deducted at source is assessable in the hands of a person other than the deductee, credit for the whole or any part of the tax deducted at source, as the case may be, shall be given to the other person and not to the deductee, provided that the deductee files a declaration with the deductor and the deductor reports the tax deduction in the name of the other person in its withholding tax returns.

It has been further provided in the Rules that the declaration filed by the deductee shall contain the name, address, permanent account number of the person to whom credit is to be given, payment or credit in relation to which credit is to be given and reasons for giving credit to such person and that the deductor shall keep the declaration in his safe custody.

It is however requested that specific inclusion of merger/demerger/amalgamation under Rule 37BA of the Rules will provide additional comfort to the deductor and create an

obligation to transfer tax credit to the resulting entity. The suggested amendment in the aforesaid Rule can help in facilitating seamless transfer of tax credit and avoid unwarranted litigation.

8.5.7 Deputation of Employees

- Increasing globalisation has resulted in fast growing mobilization of labour across various countries.
- Typically, the company deputing the personnel initially pays the salary and other costs on behalf of the company to which such personnel are deputed, which are thereafter reimbursed by the latter company.

Issue

The issue which had cropped up before the Indian tax authorities due to the increasing deputation agreements being entered cross border was whether such reimbursements made by Indian entity to an overseas entity 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.

Recommendation

- Since the employees deputed to the Indian company work under the control and supervision of the Indian company and hence are essentially ‘employees’ of the Indian company, the amounts paid by the Indian company to the foreign company are merely ‘cost reimbursements’ for the salaries paid on the Indian company’s behalf. Further, it shall be pertinent to note that the employees deputed to India pays tax as applicable for services rendered in India.
- In order to put an end to this litigation, a specific clarification may be provided by the Government to the effect that as long as the employee reports and works directly for the Indian company and operationally works under the ‘control and supervision’ of the Indian company, payments made by the Indian company to the foreign company towards reimbursement of the salary cost would be treated as ‘pure reimbursement’ and would not be taxable under the Act. It should be further clarified that such an arrangement would not trigger a creation of permanent establishment for the foreign enterprise in India.

8.5.8 Time limit for holding a Taxpayer to be an ‘Assessee in Default’ for Payments

Issues

- Section 201(3) of the Act states that no order under section 201 of the Act shall be passed holding an assessee to be in default for failure to deduct whole or part of tax from a person “resident” in India after the expiry of 7 years from the end of the financial year in which payment is made or credit is given.
- However, no such time limit exists where payment is made to a non-resident without deduction of taxes.

Recommendation

In order to provide certainty to taxpayers, it is recommended that similar time barring provisions should be introduced even in cases where payments are made to non-residents without deduction of taxes.

8.5.9 Provide for consequential amendment in section 194LC to dispense withholding obligation in respect of interest payment on rupee denominated bonds

In order to avoid litigation, in respect of exemption granted by section 10(4C) of the Act for interest payable on Rupee Denominated Bonds issued outside India between 17 Sep 2018 and 31 March 2019, suitable consequential amendment may be made in section 194LC for dispensing withholding requirement on interest income covered under section 10(4C) of the Act.

8.5.10 Apply concessional rate of WHT on trade credit when loan registration number is not applicable

Under the existing provisions of section 194LC, reduced rate of withholding tax @5% is applicable in respect of interest paid by an Indian Company on moneys borrowed from non-residents under a loan agreement or by way of issue of infrastructure bonds subject to approval of Central Government. CBDT vide circular no. 7/2012 dated 21st Sep 2012, has granted deemed approval in cases of certain Loans and Infrastructure Bonds which comply with conditions prescribed in said circular.

Issues

- One of the stipulated conditions regarding applicability of lower rate of withholding tax under section 194LC is that the loan/bonds and the rate of interest thereon have to be approved by the Central Government.
- In order to mitigate the compliance burden and hardship, the CBDT has released a Circular No. 07/2012 dated 21 September 2012 providing that any loan agreements or bond issues satisfying the conditions as mentioned in the Circular would be treated as approved by the Central Government for the purposes of section 194LC of the Act.
- While the said circular recognizes loans and bonds complying with applicable ECB regulations issued by RBI, one of the conditions is that the borrowing company should have obtained Loan Registration Number (LRN) from the RBI.
- The trade credits in nature of buyer's credit/supplier's credit are also borrowing in foreign currency and are availed through sanction letters issued by the Authorized Dealer (AD) Bank regulated by RBI. In such cases, though AD Banks are required to report such trade credits to RBI, there is no requirement to obtain any registration for same from the RBI. Hence, there is no LRN issued for trade credits by RBI and therefore, the concessional rate of withholding of 5% may be denied in such cases.
- In order to mitigate the hardship and compliance burden on borrower/issuer of bonds for taking approval in each and every specific case, the Central Board of Direct Taxes (CBDT) after enacting Finance (No.2) Act of 2014 on 6th August, 2014 issued circular no

15/2014 dated 17th October, 2014 conveying approval of Central Government to all long term bonds including long-term infrastructure bonds for original maturity period of three years of more issued on or after 1st October, 2014 to 1st July, 2017 in compliance with the specified Foreign Exchange Management Regulations. However, for subsequent amendments in section 194LC of the Act, CBDT has not issued relevant clarification for according approval of Central Government for issue of all long-terms bonds including long-term infrastructure bonds on or after 1st July, 2017 up-to 1st July, 2020 and upto 1st July, 2023.

Recommendations

- It is pertinent to note that the aforesaid concessional rate of withholding of 5% should also be made applicable to external commercial borrowings in the form of a buyer's credit/supplier's credit in foreign currency which comply with RBI guidelines and registered by participating AD Banks.
- It is suggested that suitable circular clarifying that the requirement of a loan registration number (LRN) will not apply in case of trade credits complying with extant RBI External Commercial Borrowing Guidelines and that the concessional withholding rate of 5% will be applicable to such borrowings. Further the definition of Infrastructure should be extended to core manufacturing sector such as Steel and Cement which is backbone of infrastructure.
- It is recommended to issue a circular conveying the Central Government approval to all the long-term bonds including long term infrastructure bonds for original maturity term of three years or more issued in compliance with the specified Foreign Exchange Management Regulations on or after 01st October, 2014 upto 01st July, 2023 in line with the circular no. 15 of 2014 dated October 17, 2014.
- It is also requested to extend automatic approvals to rate of interest on Rupee Denominated Bonds covered by section 194LC(2)(ia) and bonds listed on International Financial Services Centre (IFSC) recognised stock exchange covered by section 194LC(2)(ib) of the Act.

Section IX

Issues related to dispute resolution and Other Direct Tax provisions

9.1 Extend Powers of the Income Tax Appellate Tribunal to grant stay of demand beyond 365 days

Issue

Section 254 of the Act restricts power of ITAT to grant stay of demand for more than 365 days from the date of initial application, even if the delay in disposing of the main appeal is not attributable to the assessee. It has been observed that due to numerous cases involved, the main appeal remains undisposed for more than a year due to reasons not attributable to the assessee.

Hon'ble Gujarat High Court in case of ITO vs Anil GirishbhaiDarji (239 Taxman 146) and DCIT vs Vodafone Essar Gujarat Ltd. (376 ITR 23) has held that the Tribunal has the power to extend the stay of demand beyond a period of 365 days. However, extension of stay of the demand beyond the total period of 365 days from the date of grant of initial stay would always be subject to

- subjective satisfaction of the Tribunal;
- on an application made by the petitioner to extend the stay; and
- on being satisfied that the delay in disposing of the appeal within a period of 365 days from the date of grant of initial stay is not attributable to the assessee.

This provision has recently been held to be unconstitutional by the Hon'ble Supreme Court in the case of Pepsi Foods Limited [2021] 126 taxmann.com 69 (SC) to the extent the stay gets automatically vacated even if delay is not attributable to taxpayer.

Recommendation

It is recommended that provision of section 254 of the Act be amended to grant ITAT power to provide stay of demand for period exceeding 365 days where the delay is not attributable to the assessee.

9.2 Stay of Demand by the Tribunal

First and second proviso to section 254(2A) of the Act is amended by the Finance Act 2020 to provide that while granting the stay of demand or providing extension of stay of demand, ITAT shall order taxpayer to pay at least 20% of the tax, penalty, interest, fee or any other sum payable under the Act.

Issue

Tribunal, being a judicial authority, shall have the power to grant the stay considering the merits of each case. Imposing a condition of directing ITAT to ask taxpayer to deposit at least 20% of tax, interest, penalty, fee or any other sum payable under ITA will result in undue hardship to taxpayers especially in case of high pitch demands and where the substantial question of law is arising in the appeal.

Recommendation

First and Second proviso to section 254(2A) of the Act may, therefore, be omitted and discretionary powers available with ITAT in granting stay should be continued.

Without prejudice to above, discretionary powers should be granted to ITAT to depart from statutory mandate to grant stay in exceptional high pitch demands based on the merits of the case and cases where substantial question of law is under consideration.

Further, the percentage of pay-out should be restricted to disputed tax demand and should not be extended to disputed interest and penalty amount

9.3 Pre-deposit limit for stay of demand at the first appeal stage be reviewed and reduced to 10% of the disputed amount

CBDT had earlier vide office memorandum dated 29 February, 2016, modified the guidelines for stay of demand at the first appeal stage issued under Instruction No. 1914 of 1996. CBDT made it mandatory for the tax officer to grant stay of demand once the taxpayer pays 15% of the disputed demand, while the appeal is pending before the Commissioner of Incometax (Appeals). CBDT vide office memorandum dated 31 July, 2017, has further modified Instruction No. 1914 of 1996 and has revised the standard rate prescribed in the office memorandum dated 29 February, 2016, from 15% to 20% for grant of stay at the first appeal stage.

It may be noted that the reasons stated in the office memorandum dated February 29, 2016 modifying the guidelines stated in Instruction No. 1914 dated 21.03.1996 was that "It has been reported that the field authorities often insist on payment of a very high proportion of the disputed demand before granting stay of the balance demand. This often results in hardship for the taxpayers seeking stay of demand". Para 4 of the aforesaid memorandum further stated that "In order to streamline the process of grant of stay and standardize the quantum of lump sum payment required to be made by the assessee as a pre-condition for stay of demand disputed before CIT(A), the following modified guidelines are being issued in partial modification of Instruction No. 1914:"

Thus, the basic objective for modifying the Instruction No. 1914 (supra) and prescribing a payment of 15% of the disputed demand was to reduce the hardship for the taxpayers seeking stay of demand. The memorandum dated February 29, 2016 further provided situations which warranted payment of a lump sum amount higher than 15% (e.g., in a case where addition on the same issue has been confirmed by appellate authorities in earlier years or the decision of the Supreme Court or jurisdictional High Court is in favour of revenue or addition is based on credible evidence collected in a search or survey operation etc.) [Para 4B(a)]. On the contrary, CBDT has increased the pre-deposit limit from 15% to 20% vide office memorandum dated 31 July, 2017 stating that the standard rate of 15% prescribed earlier was found to be on the lower side. It is observed that the increase in predeposit limit from 15% to 20% without any reasonable justification in all the cases (taxpayers whose case does not fall in para 4(B)(a)) will lead to hardship for the genuine taxpayers.

Recommendation

It is suggested that the pre-deposit limit for stay of demand at the first appeal stage be reviewed and reduced to 10% of the disputed amount.

Further, in case of matters which are already covered in the favour of assessee (by virtue of favourable Tribunal or High Court orders), it should be clarified that, such demand should not be adjusted under section 245 of the Act against refunds due to the taxpayer for any other years as held by various High Courts . Also, merely because the tax department has filed an SLP before the Supreme Court should also not be a ground for not allowing the stay of demand (in cases where issues are already covered in favour of taxpayer by High Court orders).

The above clarifications will certainly provide a much needed relief to the taxpayers who are generally hard pressed by the field officers for recovery of demand despite of the fact that the issue is covered in their favour in earlier years.

Further, it should be clarified that the aforesaid Memorandum should be applicable even in cases where appeal is pending before the Income-tax Appellate Tribunal (which is as such the first appellate authority for taxpayers opting for the DRP route).

9.4 Requirement to obtain Permanent Account Number by non-individual entities entering financial transactions

Section 139A of the Act casts an obligation on every person to obtain a Permanent Account Number (PAN) under certain prescribed situations. Such situations are enumerated in clauses (i) to (iv) of sub-section (1) to section 139A of the Act. The Finance Act, 2018 inserted the following two new clauses viz. (v) and (vi) in section 139A(1): "Every person, -

(i)…..

(ii)….

……..

(v) being a resident, other than an individual, which enters into a financial transaction of an amount aggregating to two lakh fifty thousand rupees or more in a financial year; or

(vi) who is the managing director, director, partner, trustee, author, founder, karta, chief executive officer, principal officer or office bearer of the person referred to in clause (v) or any person competent to act on behalf of the person referred to in clause (v)

(vii) who intends to enter into such transaction as may be prescribed by the Board in the interest of revenue and who has not been allotted a permanent account number shall, within such time, as may be prescribed, apply to the Assessing Officer for the allotment of a permanent account number".

Issues and Recommendations

Taxpayer who "intends" to undertake certain specified transactions to obtain PAN

- The additional circumstance added in section 139A(1) by Finance (No.2) Act 2019 is that the taxpayer will have to obtain PAN if taxpayer "intends" to enter into such transactions as may be prescribed by Board in the interest of revenue.

- There is ambiguity in language of the provision. Literal reading would mean that provision requires taxpayer to obtain PAN merely on the basis of 'intention' of Taxpayer to undertake prescribed transaction, irrespective whether or not the transaction is actually undertaken/consummated.
- A suitable amendment should be made to bring out that person is liable to obtain PAN before entering into or execution of prescribed transactions.

9.5 Set Off of Refunds against Tax remaining Payable

Issue

- Adjustment of refunds due to assessees against erroneous demands shown outstanding in their cases causes great heartburn. Even where the assessee lodges his objection on the CPC portal pointing out that the demand sought to be adjusted against the refund was not outstanding and therefore is being erroneously adjusted, there is no remedy by which the CPC can take note of the same.
- It is settled by several judicial pronouncements that where any demand outstanding against the assessee relates to a point which stands squarely covered by a decision in the assessee's favour, such demand cannot be adjusted against any refund due to the assessee. Courts have logically explained in this regard that the assessee in such a case would have been undisputedly entitled to stay on recovery of such demand, and merely because the department is in possession of the assessee's funds due to him as legitimate refund, it cannot be adjusted against such a demand.

Recommendation

- It is suggested to amend the section so as to provide that no set-off of refund under this section shall be made by any income-tax authority without giving intimation in writing to such person of the action proposed to be taken under this section, and without dealing with the objections, if any, filed by such person in response to such intimation served on him. Systems should be amended/put in place to stop assessees' funds being adjusted without authority of law. It is further suggested that proper guidelines be laid to introduce accountability and further avoid overlapping of responsibility between TRACES/CPC officers vis-à-vis the jurisdictional officers in such cases. It is further suggested that refund struck with the department due to adjustment against erroneous demand, non-grant of due TDS credit etc. be made eligible for interest @ 12% per annum.

9.6 Restriction on Set-off of Loss from House Property

The Finance Act, 2017 has inserted sub-section (3A) in section 71 of the Act to provide that loss from house property up to Rs. 2 lakhs only will be set-off against the income under other heads in the same financial year. Loss above Rs. 2 lakhs is eligible to be carried forward for a period of eight years and can be set-off against income from house property only.

Issues

- This provision contradicts with the intention of the government to incentivise housing sector and promote investment in real estate sector. This could act as a dampener for promoting investment in the Housing sector.
- Considering that in most of cases, the prices of properties have gone down by more than 20-25% in the past 3 to 4 years, the owners are already burdened with the reduction in the value of property combined with interest cost. This provision would further compound the misery of the owners as apart from the huge loss of capital and outflow of interest, their tax burden would also increase substantially.
- Generally, middle class and lower middle-class people invest in property by obtaining loan from banks. The amount of interest paid is always higher than rental income earned from such property.
- The owners of the property had entered into these loan arrangements for purchase of the property based on the prevailing tax provisions at that time and change in the prevailing provision in respect of loans taken before the change would have retrospective implications as the owners are not in a position to reverse the transaction.
- As a specific example, it discourages the middle class from investing in a house property as a backup post retirement (including government employees) (where the house may be let out temporarily). Further, the amount of Rs. 2 lakhs as interest threshold is quite low compared to interest payout made by the taxpayers in initial years of loan. The above threshold should be at least increased to Rs. 4 lacs.
- Further, the loans are obtained for 15-20 years and the interest payments in EMIs are very high until 10th year. In eight years, they will not be able to set off the interest resulting in permanent loss to them.
- The limitation of house property loss set off upto Rs. 2 lakhs also adversely impacts the real estate developers holding unsold inventories of flats/units. As per s.23(5), the annual value of unsold inventory for real estate developers is taken as NIL for a period upto 2 years from the end of the financial year in which completion certificate is received. This implies that such property will be liable to house property taxation from the year of its completion till its sale. The real estate developer usually borrows substantial amounts for real estate development project. ICDS IX requires capitalisation of such interest cost to the real estate project inventory value. The limitation on house property loss set off precludes the real estate developer from deducting the interest cost on unsold inventory against profit from sale of such units. For instance, if the real estate developer has constructed 10 units and sells 6 units in Year 1 and balance 4 units in Year 2. The interest cost pertaining to 4 units sold in Year 2 is not permitted to be set off against profits of 6 units in Year 1 (since the set off is restricted to a nominal amount of Rs. 2 lakhs) and even after carry forward of such loss to Year 2, it is not allowed to be set off against the profit on sale of same 4 units. This leads to highly unjust result and a very high tax cost for real estate developers.

Recommendations

- The limitation provided by the Finance Act, 2017 limiting the set-off of loss of house property to the extent of Rs. 200000 should be removed.
- It is observed that the amendment has a retrospective effect which is against the commitment made by the Government to not make any retrospective amendment. If any change is required to plug the tax benefit, it is recommended that houses purchased after 1 April 2017 or housing loans obtained after the said date should be covered under the provisions of section 71(3A) of the Act and suitable amendment be made accordingly.
- It should be further clarified that interest deduction for self-occupied property and let out property, a separate limit of Rs. 2 lakh each, aggregating to Rs.4 lakh should be made, so that the interest deduction for self-occupied property and let out property both is available to the extent of Rs. 2 lakh each. Alternatively, the time limit of eight years should be removed for carry forward and set off and the loss should be allowed for an indefinite period like unabsorbed depreciation allowance.
- In any case, an exception should be carved for unsold inventories of real estate developers to which such limitation should not be applied at all.

9.7 Computation of advance tax to include deductibility of Foreign Tax Credit (FTC)

Issue

- Section 209(1)(d) of the Act provides that while computing the advance tax payable, income-tax which would be deductible or collectible at source during the financial year under the provisions of the Act from any income which has been taken into account in computing the current income shall be reduced from the advance tax so computed. However, the current provisions of Section 209 of the Act do not cover deductibility of foreign tax credit in the computation of advance tax payable.

Recommendation

- Section 209 of the Act should be amended to expressly provide for deductibility of FTC in addition to taxes deductible or collectible at source from the advance tax computation.

9.8 Calculation of Interest for delay in Deposit of Taxes deducted - meaning of 'Month' – 'month' be defined as a period of 30 days

Issue

- As per Section 201 (1A) of the Act, interest on late deduction of TDS is calculated @1% for every month or part of month from the date on which tax was actually deductible to the date on which tax was deducted and interest on late deposit of TDS is calculated at 1.5% for every month or part of month from the date on which tax was deducted to the date on which tax is actually paid. However, for the purpose of calculating period of delay, the Revenue Authorities calculate interest on a calendar month basis. For

instance, where tax was deductible on 30 June and the tax so deducted was remitted on 8 July, interest has to be paid for June and July (i.e. 2 months) for a one day delay.

Recommendation

- In order to mitigate this hardship caused to the taxpayer, it is suggested that 'month' be defined as a period of 30 days to avoid litigation on this issue. This would make the reckoning of period while interpreting the tax law more meaningful and clear.

9.9 Inclusive Method of Accounting - Section 145A

Issue

- The conflict in the provisions of Section 145A of the Act and the Accounting Standards notwithstanding its nil impact on the Profit and Loss or taxable income has transformed itself into long drawn unwarranted litigation.

Recommendation

- It is recommended that provision of Section 145A of the Act be amended to fall in line with the Accounting Standards.
- Alternatively, it is recommended that the said provision be deleted, since in ultimate analysis, there is no revenue implication.

9.10 Filing of return of income

Issue

- Various positions are taken by the taxpayer at the time of filing the return of income. However, due to the limitation in the format of the income tax return/form, the taxpayer is not able to provide all disclosures in respect of the positions taken by him in the return which has impacted the computation of income/loss of the taxpayer.

Recommendation

- It is recommended that the income tax return form should be appropriately modified to provide adequate space for writing notes to the return of income.

9.11 Deduction to be allowed on merits even if claim is not made in tax return

Issue

- Section 80A(5) of the Act denies deduction to an assessee, in case he has failed to make a claim in his return of income for any deduction under sections 10A, 10AA, 10B, 10BA or under any provision of Chapter VI-A under the heading “C- Deductions in respect of certain incomes”. Provisions are highly punitive and are applied even in case of bonafide assessees. As per Circular No.14 dated 11/4/1955 the assessing officer is bound to allow deduction even if the same has not been claimed by the assessee. It is a settled law that beneficial provisions/deductions etc. should be interpreted liberally. Various High Courts have consistently ruled that if an assessee has omitted to make a claim in tax return, then the same can be made during the course of assessments/appellate proceedings. However, the tax officers reject the claims made by the taxpayers during the course of

the assessment proceedings which are omitted to be claimed by the latter in their return of income.

Recommendation

- The Act should be suitably amended to specifically state that a taxpayer can make claim for any exemption, deduction, set-off or any other relief at the time of assessment proceedings as well and such claim should be regarded as having made in the return of income for the purposes of the Act.

9.12 Authorised Signatory for the purpose of signing of return and appeals

Issue

- In case of a company, the tax return and appeal documents to be filed before CIT(A) and ITAT are required to be signed by the Managing Director or any other director (only in case Managing Director is not available for unavoidable reasons) as per Rule 45(3) and rule 47(1) of the Rules read with section 140 (c) of the Act.
- Vide Finance Act 2020, necessary amendments have been made in Section 140 (c) of the Act empowering the Board to specify by rules any other authorised person to sign the aforesaid Returns/Appeals. In case of return filing under the indirect taxation, any authorised signatory of the company can sign the company's returns.

Recommendation

- It is requested that CBDT should issue necessary Notification/Circular to enable any signatory, who is authorised by way of a Resolution passed by the Board of Directors of the company, to sign the Returns, Appeals, and all other documents under the Income Tax Act so as to give effect to the amendments in Section 140(c) made vide the Finance Act 2020.

9.13 Tax effect of Appellate Orders

Issue

- It is often observed that the assessing officers do not provide tax effect of appellate orders favourable to assessee for long period of time. Lot of follow ups and reminders are required to get refunds. Further, considering the fact that there is a time limit for payment of tax, filing returns, completing assessment, etc., there should be a provision mandating the assessing officer to grant refund within certain specified days of receipt of appellate orders.

Recommendation

- It is suggested that there should be provision in Income Tax Act to make assessing officer accountable to grant refunds within 30/45 days of receipt of appellate order.

9.14 Provide exemption from levy of interest under section 234C on interest on income tax refund

Issue

- Interest under section 234C of the Act is levied for earlier quarters where interest on income tax refund is received during the year. It is a settled law that interest on income

tax refund is chargeable to tax only on actual receipt. This causes hardship to the taxpayers since he is required to pay interest for the period for which he has not received any income. The charging of interest should be aligned with the time of receipt of interest income on income tax refund.

Recommendation

- Suitable amendment be made in section 234C of the Act to provide exemption from levy of interest on interest income on income tax refund for the period/quarter prior to receipt of such refund.

9.15 Prescribe mandatory time limit for processing of rectification and stay applications

Issue

It has been observed that the rectification application and stay applications filed by the taxpayers are not processed timely by the tax officers due to which the tax payer is refrained further taking further action and the environment of uncertainty is developed. The taxpayers also suffer from actions of the tax officer such as notice for additional demands, coercive recovery, and unnecessary pressure to pay demands. This causes serious liquidity problems for the taxpayers.

Recommendation

It is suggested that a statutory mechanism for ensuring disposal of rectification and stay application filed by the taxpayers within a prescribed time limit should be introduced. It is further suggested that amendment be made in section 154 of the Act to provide that in case the tax officer does not pass the rectification order within a specified period of say 6 months from the date of filing of application, rectification application shall be deemed to be allowed. Further, similar provision should also be introduced in the Act to ensure timely disposal of stay applications filed by the taxpayers.

9.16 Prescribe 12% rate of Interest on Tax Refunds under Sec 244A

Issue

Under section 244A of the Act interest is computed @ 6% per annum on tax refunds payable by the Government however in cases of interest payable by the assessee to the Government, such as in section 234B, rate is 12% p.a. Money has only one colour and therefore the rate of interest may be same irrespective of whether interest is paid to the department or received from the department.

Recommendation

A uniform rate of interest of either 6% or 12% p.a. both for refunds and tax dues payable by the Government and assesses respectively may be prescribed.

9.17 Time limit for furnishing of quarterly TCS return in form 27EQ should be aligned in line with Form 24Q

- As per Rule 31AA of the Rules read with sub-section (3) of section 206C of the Act, every collector has to file in a quarterly statement in Form No. 27EQ by 15th day from the end of each quarter. Statement for quarter ending March shall be file by 15th May.
- However as per Rule 31A of the Rules read with sub-section (3) of section 200 of the Act, every person responsible for deduction of tax under Chapter XVII-B shall file a quarterly statement in Form No. 24Q, 26Q and 27Q by 31st day from the end of each quarter. Statement for quarter ending March has to be filed by 31st May.

Issues

- After implementation of Section 206C(1H) and Section 194Q, where the turnover of the buyer is more than Rs. 10 Crore in the previous Financial Year, buyer needs to deduct TDS under section 194Q and in such case seller needs to report buyer challan number and challan date in his TCS return. However, where buyer fails to deduct the TDS, Seller needs to collect TCS on the same.
- This requires the seller to reconcile his sale with the buyer and to take buyer challan number and challan date. After reconciliation seller needs to deposit the TCS where buyer has not deducted TDS.
- The above activity requires lots of time and efforts in compilation of information for filling the TCS return in Form 27EQ.

Recommendations

- The time limit for furnishing of quarterly TCS return in form 27EQ should be increased in line with other Form 24Q, 26Q & 27Q i.e. to 31th of next quarter except March wherein the time line is 31st May of next year.

9.18 Due date of deposit of Tax Collection at Source for March should also be extended from 7th April to 30th April

As per the Rule 30 of the Rules all sums deducted in accordance with the provisions of Chapter XVII-B by deductor shall be paid to the credit of the Central Government on or before seven days from the end of the month, in case of March month on or before 30th day of April.

- However as per Rule 37CA, Tax Collection at Source shall be paid to the credit of the Central Government on or before seven days from the end of the month.

Issue

- Along with other section, seller has to collect TCS on his sale of goods under section 206C (1H) which takes much time in line as calculation of TDS liability. Further where buyer is required to deduct TDS, seller is not required to collect TCS but if buyer fails to deduct TDS then seller needs to collect TCS. This involves lots of time and efforts to reconcile the data with the details of TDS deducted by buyer.

Recommendation

- Due date of deposit of Tax Collection at Source for March should also be extended from 7th April to 30th April like in case of deposit of Tax Deduction at Source.

9.19 Rationalization of procedures followed by Centralised Processing Centre ('CPC')

(a) Issue of refunds to non-residents

Issue

In many cases, where the refund amount is in excess of Rs. 50,000, the refund is not credited directly into the assessee's bank account but the cheque is sent to the physical address in India. In many cases, the non-resident may not have an address in India or the non-resident individuals may have sold the only house he had in India but has not yet changed the address in the PAN records for want of time or for want of the supporting documents required for the change of address in PAN records (especially w.r.t. attestation of documents). Even in those cases where the non- resident has an address in India and the cheque is duly delivered at that address, it cannot be deposited into the bank account because it requires the assessee to sign behind the cheque and fill up certain details. This results in the cheques lying uncashed and then becoming outdated.

Recommendation

It is suggested that all refunds should be credited directly into the bank accounts of the assessee instead of a physical cheque being sent.

(b) Non-granting of credit for TDS

Issue

Often, the TDS that appears in the Form 26AS for Year 1 is not claimed by the tax payer in his return of income for that year but is claimed in Year 2. In such cases, in Year 1, the TDS is shown as carried forward to Year 2 and in Year 2, it is shown as brought forward from Year 1. This primarily happens in cases of professionals, where the assessee follows the cash method of accounting and the deductors follows the accrual method of accounting. Despite this facility being made available in the ITR forms to carry forward the TDS to the subsequent year, the intimations under section 143(1) of the Act are received for the Year 2 where credit is not given for the TDS. Upon filing application for rectification under section 154 of the Act, the same working is received back by the assessee without any change in the TDS credit. The reason given in the order under section 154 of the Act for rejecting the application is "Credit claimed does not match with 26AS". At the same time, in such rectification orders, interest under section 244A granted earlier is reduced and this in turn results in a demand being raised on the assessee. Subsequent rectification requests are also rejected with identical reason and demand.

Recommendation

It is suggested that the systems of CPC be updated immediately to overcome this issue.

(c) Adjustment of old demands against recent refunds

Issue

It has been noticed in many cases that suddenly, some very old demands are shown to be outstanding against the assessee. In such cases, for demands of some of the earlier years, one can download the AO's computation sheet but for some years, these sheets are not available. In such situations, the assessee has to then personally follow up with the jurisdictional AO's office for the computations. If the matters pertain to very old years, it becomes very difficult to locate the records and obtain copies. As a result, the refunds due to the assessee get locked up for several years.

Recommendation

It is proposed that as soon as a demand is uploaded onto the system, the assessee should get a notification so that he/she can immediately take action in the matter instead of having to do so after a few years.

(d) Filing of returns by taxpayers covered by presumptive taxation

Issue

Taxpayers offering income on presumptive basis are not required to maintain books of accounts. However, they may have a PE in India for the year, but have opted to offer tax under the presumptive taxation regime. However, while processing the return of income, CPC issues notice under section 139(9) of the Act proposing to treat the return of income as invalid as the Balance Sheet & Profit and loss account details are not filled up.

Recommendation

It is recommended that the CPC takes remedial action in cases mentioned in the Justification section and does not treat the returns as defective.

(e) **Provide for suitable procedure for demand raised by CPC under section 220(2)**

Issue

In the status of Outstanding Demands under the Income Tax e-filing portal, CPC also updates separate demand amounts as payable under section 220(2) without issuing any separate Speaking Order and separate Demand Notice under section 156 to the assessee.

Also, such demand amounts under section 220(2) of the Act are recovered by CPC from the Refunds arising out of intimation under section 143(1) processed by CPC for other year.

By not issuing separate speaking order along with separate demand notice under section 156 of the Act for such separate demand amount under section 220(2) updated on e-filing portal by CPC, the assessee is deprived of filing any Appeal against such Demand in absence of any Appealable Order, which is unjustified.

Recommendation

It is requested to make suitable procedure so that separate demands are not directly updated by CPC on the e-filing portal and such demands under section 220(2) of the Act are

raised only by the jurisdictional Assessing Officer by way of issuing separate Appellable/Speaking Orders along with separate demand notice under section 156 of the Act.

9.20 Direction for Special Audit under sub-section (2A) of Section 142 of the Act

The Finance Act, 2013 has made an amendment to Section 142(2A) of the Act which widens the power of the Assessing Officer to direct the taxpayer to get accounts audited and furnish the report in certain circumstances. The expression "nature and complexity of the accounts" has been replaced with the "nature and complexity of the accounts, volume of the accounts, doubts about the correctness of the accounts, multiplicity of transactions in the accounts or specialized nature of business activity of the assessee".

Issues

- The amendment seeks to enlarge the scope of Section 142(2A) of the Act and gives sweeping powers to the assessing officer to direct special audit in most of the cases.
- The conditions prescribed for referring the case for special audit are not inter dependent i.e. even one of the conditions could trigger recommendation for special audit. The applicability of this provision merely on the basis of volume of the accounts or multiplicity of transactions in the account is unreasonable since in such a case, all big companies with voluminous transaction could be referred for special audit.
- Reasons such as volume of accounts, multiplicity of transactions in the accounts, specialized nature of business activity of taxpayer etc. are not defined categorically to state the quantum/ threshold etc. for initiating a special audit.

Recommendations

- Applicability of this provision should not be invoked merely on the basis of volume of the accounts or multiplicity of transactions in the account. The provision should be amended to require satisfaction of all the conditions cumulatively for directing for special audit under Section 142(2A) of the Act.
- The terms such as "volume of accounts", "multiplicity of transactions in the accounts" and "specialized nature of business activity of assessee" would need to be defined very clearly in the Section in order to avoid litigation/ ambiguity in the interpretation of the Section.

9.21 Waiver of interest under section 201(1A) – circular no. 11 of 2017 to be codified

Issue

CBDT circular no. - 11/2017, dated March 24, 2017, has issued guidelines wherein CBDT has provided powers to Chief Commissioner of Income-tax/Director General of Income-tax to grant waiver of interest under section 201(1A) where *inter alia* application has been filed under MAP, subject to specified conditions. The above benefit should also be extended to the assessee who have filed application before Authority of Advance Ruling and Advance Pricing Agreement. In case of AAR, time limit of six months for passing of an order has been

prescribed in the Act, however, it has been observed that due to practical challenges, AAR proceedings have taken more than five years in most of the cases.

Recommendation

In view of the above, provision must be inserted in the Act to grant powers to CCIT and DGIT to grant waiver of interest under section 201(1A) to entities who have accepted the ruling of MAP, AAR or APA. The waiver of interest shall be from the date of filing application for MAP, AAR or APA till the receipt of the order from respective authorities. Alternatively, CBDT could issue new circular providing similar benefit to persons filing application with AAR or APA.

9.22 Suggestions to minimise litigation

a) Create a separate vertical in Tax Administration for handling litigation before Tribunal, BAR, High Courts and Supreme Courts. The involvement of specialised vertical will significantly improve the quality of pleadings and arguments on behalf of Tax Department, minimise litigation on frivolous issues, act as a check against unwarranted high- pitched additions and initiation of penalty in a mechanical manner.

b) Due to the current four years pendency of AAR cases and abolition of AAR & its replacement by Board for Advance Rulings (BAR) by Finance Act 2021, following should be considered**:**

- Increase number of benches at BAR
- Rulings should be pronounced in a time bound manner – six months
- Composition of Members of BAR should be relooked at Expand eligibility criteria for Members and external experts should be included
- Dedicated bench should be constituted for public sector undertaking matters

c) A Court assisted conciliation process should be introduced. This would facilitate reducing quantum of appeals being filed at higher forums. Illustrative model - Mandatory conciliation process should be resorted to after the Tribunal's order, in cases where tax effect is less a monetary threshold (say Rs 10 crores)

d) Supreme Court o Dedicated tax bench should be constituted which should hear matters on a daily basis. This would increase the number of cases being disposed off and reduce the overall litigation timeframe

e) High Court o Norms for filing appeal to High Court should be made stricter for the Income-tax department. This would reduce the number of appeals being filed at the higher forum

f) Tribunal o Strict norms (including restrictions on number of adjournments) should be prescribed for Department seeking adjournments before Tribunal in stay granted matters

- If appeals are not adjudicated within a specified time period on account of Department seeking adjournments, taxpayers should not be asked to pay outstanding demands

g) Statutory time limit of 90 days for passing order from the date of conclusion of hearing seems to be stringent having regard to current case pendency status at ITAT and hence, time limit may be suitably increased to 180 days.

h) Statutory time limit of 2 years for disposing appeals by Tribunals should be introduced instead of present persuasive time limit of 4 years.

i) Create online repository of case status and pending issues at different levels which will assist both Tax Department and taxpayers to ascertain status of similar issues in past appeals.

j) Empanelment of competent lawyers to protect public interest

k) Capacity building measures where Departmental Representatives should be appointed for a fairly long time (say 5 years), there should be regular training programs for tax officials

l) The CBDT should frequently issue Circulars or FAQs on contentious issues for the guidance of AOs so that they do not take any positions or file appeals contrary to the CBDT's views

m) Expand scope of section 158A and section 158AA to permit 'tagging' with similar issues in other taxpayer's cases

n) Make revision orders passed under section 264 of the Act by Commissioner of Income-Tax appealable to Tribunal

o) Liberalise immunity from penalty under section 270AA of the Act - taxpayer may be permitted to seek immunity on select issues by paying up tax and interest thereon while permitting him to contest other issues in further appeal, scope of immunity under section 270AA of the Act may be expanded to any assessment order passed on or after the date of amendment.

p) The CBDT should provide clear guidance to AOs on circumstances in which penalty should not be initiated.

q) Taxpayers' Charter

- A timeframe should be provided in respect of every action to be undertaken by the Income-tax department e.g. Commissioner (Appeals) to pass order within one year from end of financial year in which appeal is filed [Section 250(6A)]
- Introduction of legislative safeguards for protecting taxpayer's data
- A rider should be included to the effect that information/ data collected by the Income-tax department would be used only for the purposes for which such data is collected

- Taxpayers should be provided an option for their decisions/ rulings to be published on anonymous basis. This would protect taxpayers' reputation in public domain

9.23 Withdrawal of registration of charitable trust in case of non-compliance of 'material' conditions of other applicable laws – Section 12AA

(i) Section 12AA of the Act is amended by Finance (No.2) Act 2019 to provide that registration of charitable trust can be cancelled in case of non-compliance of 'material' conditions of other applicable laws.

(ii) The above requirement should be deleted for the following reasons

- Adequate provisions under the Act to cancel registration of non-genuine charitable trusts or where activities are not in line with the objects of the trust.
- The respective authorities under other laws have enough powers/rights to take action against the trust for not abiding by the respective law
- It may not be a correct practice to implement other laws through the Act.
- Determination of 'material' non-compliance is subjective and increases scope of litigation.

9.24 Tax on buyback of shares in case of listed companies

Finance Act, 2019 has amended section 115QA of the Act to include such tax on buyback of listed shares.

- Buy-back tax (BBT) under section 115QA of the Act was introduced to counter-balance Dividend Distribution Tax (DDT) levied under section 115-O of the Act. Hence, with abolition of DDT vide Finance Act, 2020, corresponding levy of BBT is not justifiable.
- Without prejudice to the above, the scope of applicability of the buy-back tax provisions should be narrowed down to exclude certain kinds of listed entities which fulfill stipulated objective criteria/parameters indicative of the genuine cases where the buyback may not be considered to have been undertaken as a tax avoidance exercise, for companies having a steady dividend pay-out record, achievement of certain performance parameters such as EPS, Return on Equity, Return on Capital, Debt-Equity Ratio, etc., companies which are in immediate need of funds, etc.
- In case of open market buy back offer through stock exchange, the shareholders offering their shares under buy back would not be able to claim exemption under section 10(34A). In all other cases of buy back, the shareholders are aware that they are tendering their shares to the company under buy back mechanism and hence their transaction is exempt from tax under section 10(34A) of the Act. However, under open market buy back, the shareholders are not aware since transaction in stock exchange happens normally like purchase and sale of shares based on the bidding mechanism. Hence, shareholders would be paying capital gains tax on the same transaction on which company has paid Buy back Tax which results in double taxation of the same income. It is a well settled principle that no provisions of the Act can be so interpreted that it results in double taxation.

- The primary objective of Buy Back through open market offer in stock exchange is to provide support to the share price, in a fluid or uncertain market. Free fall of share prices, in such a situation, could provide an opportunity to unscrupulous operators (including from overseas) to buy shares at throw away prices, at the cost of public investors, who may go for panic selling. Thus, it is of great importance in the present time, to reduce the scope of BBT under section 115QA to exclude Buy Back under Open Market offer through Stock Exchange. This would encourage more listed companies to resort to buy back mechanism when economy if facing an extremely uncertain future on account of COVID-19 virus pandemic.
- As per Sec. 115QA read with Rule 40BB of the Rules, buy back tax is chargeable on distributed income (i.e. difference between the consideration paid to the shareholders and the amount received at the time of subscription of shares). The fact that listed shares are frequently traded is totally ignored in this computation mechanism. Thus, levy of BBT on listed companies result in indirect double taxation since the computation mechanism does not consider the fact that the shareholder may have purchased the shares at a rate higher than the issue price & it may so happen that all the previous transfers would have already been taxed in the hands of the shareholders under Capital Gain.
- Grandfathering provisions to be introduced under Section 115QA of the Act or Rule 40BB of the Rules akin to section 55(2)(ac) of the Act from company's perspective such that the "amount received" for the purpose of determining "distributed income" under Section 115QA of the Act may be deemed to be the market price of shares prevailing on stock exchange as on 4 July 2019.

9.25 Deeming Fair Market Value as Full Value of Consideration for Transfer of Unquoted Shares

Currently, section 56(2)(x) of the Act provides that where any person receives any sum of money or property without consideration or for a consideration less than Fair Market Value (FMV), the recipient may have to pay tax on the basis of FMV. Further, section 50CA of the Act provides that where unquoted shares are transferred at a price less than FMV, consideration for the purpose of computing capital gains in the hands of seller shall be deemed to be the FMV. For both these provisions, FMV is determined on the basis of the prescribed method.

Section 56(2)(x) and 50CA of the Act has been amended by the Finance Act, 2019 to restrict its applicability on prescribed transactions undertaken by certain class of persons, which shall be prescribed by the CBDT. Such amendment is intended to remove genuine hardship in cases where consideration for transfer of shares is approved by certain authority and person transferring the share has no control over such determination.

Over the past few years, several measures have been put in place to target certain abusive transactions and arrangements. The General Anti-Avoidance Rule (GAAR) is by far the most important and prominent of these, but there have been several more targeted anti-abuse provisions that have been introduced in recent times, which are posing several challenges to

industry. The most serious of these relate to sections 56(2)(x) and 50CA of the Act. As aforesaid, these seek to bring to tax notional incomes in the hands of the recipient and transferor in cases where the transaction takes place at a price lower than a specified fair market value.

Although the need to target abusive transactions is undoubtedly an important objective, it is submitted that such provisions are so far-reaching in their scope that several ordinary and legitimate commercial transactions end up triggering significant tax costs. Since these are taxes on notional, rather than real income, they end up significantly increasing tax costs for businesses. For instance, commercial negotiations based on innumerable factors affect the pricing of shares and other assets. To tax such transactions merely because the negotiated prices differ from the price determined on the basis of a statutory formula is unduly harsh, especially since they apply to unrelated parties as well. With the GAAR now in force, specific abusive transactions can be appropriately targeted under its provisions, without having to resort to such catch-all provisions. We therefore submit that both sections 56(2)(x) and 50CA be deleted.

Other Issues

- Under an approved Resolution Plan under Insolvency and Bankruptcy Code, 2016 (IBC), there could be several instances where assets (including shares) of a company are transferred in distress. However, the aforesaid provisions could render many such transactions as unviable, both from a sellers' and buyer's perspective in cases where the prices are lower than the formula based approach set out in section 56(2)(x) and 50CA of the Act. For e.g., a buyer may have to pay tax on the difference between book value and purchase consideration, when in fact no gain/benefit has been received by the buyer who is already taking a significant risk by investing in distressed businesses. On the other hand, the seller may have to pay capital gains on the difference between FMV and the sale consideration, when in fact the seller is actually incurring a loss. In many cases, the tax cost itself may be higher than the sale/purchase consideration. This is grossly unjust and could deter business sentiment and undermine the policy objectives particularly at a time when the Government is trying to revive the distressed sector.

- In case where the shares are acquired under SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, offer price of the shares is determined much prior to the date of acquisition of shares on account of offer period to the public. Similarly, in case where a transaction requiring approval from regulatory authority (SEBI, RBI, IRDA etc.)

  for transfer of shares, the date of acquisition is different from date of agreement fixing the consideration for shares. Exemption on the lines of immovable property provided under section 50C and 56(2)(x)(b) of the Act may also be provided for acquisition of shares.

- Definition of 'quoted shares' present in section 50CA of the Act suggests that shares of company which are listed outside India may be considered as 'unquoted shares'. On transfer of shares of company listed outside India may also call for determining the fair market value in terms of Rule 11UAA of the Rules. It is practically impossible to obtain

the Balance Sheet of foreign companies on the date of transfer of shares. Further, it is not possible to obtain the Balance Sheet of companies whose shares are held by such foreign companies for computing FMV as per Rule 11UAA of the Rules.

- The literal interpretation of section 56(2)(x) of the Act will make all genuine transactions like allotment of shares under initial public offer (IPO), follow on public offer (FPO), contribution of assets into a partnership firm, issue of bonus shares, issue of right shares to existing shareholders or infusion of further capital, preferred allotment of shares, disinvestment of PSU by Govt. of India, etc. taxable in the hands of recipient as they are less than fair market value, to attract investors. In the above scenarios, the shares (being covered by the definition of 'property') comes into existence only on allotment of such shares and therefore question of receipt of such shares from any other person (something which is non-existing) is not possible. It is in fact an allotment of fresh shares by the Company and not a transfer of shares by one shareholder to another shareholder. Thus, capturing allotment of shares within the purview of section 56(2)(x) of the Act does not seem to be the intent of the Government and needs to be clarified.
- The provisions of section 56(2)(x) are not applicable in case of transfer of property or assets (such as shares or securities) from a relative, whereas in the case of transfer of shares to a relative for lower consideration or nil consideration, the differential between FMV and transfer price becomes taxable in the hands of transferor under section 50CA of the Act.
- CBDT has issued final rules for the determination of fair market value (FMV) of unquoted equity shares for the purposes of section 56(2)(x) and section 50CA of the Act. The rules for valuation of unquoted equity shares have been introduced as anti-abuse provisions, intended to curb transfers of unquoted shares at nominal value despite such shares holding underlying assets of substantial value. However, it would be inequitable to apply the rule prescribing fair market valuation of underlying assets; in cases where control in the company has not changed. The genuine cases of internal restructuring wherein the ultimate ownership does not change should be provided exemption from adopting fair market value. It is observed that adopting the fair market value of the underlying assets would be inequitable in case of rearrangement within the same owner group as the essence of the transaction is not intended as a pure sale in such cases. It has to be appreciated that it would be impossible for a minority shareholder to be able to materialise the transaction based on fair market value of the underlying assets. Practically, a nominal shareholder may not have access to such information and hence, may not be able to compute value according to this rule. It has also to be appreciated that the information pertaining to the assets of the unlisted company like immovable property, jewellery etc. would not be available in public domain and would pose serious challenges in complying with the valuation mechanism as prescribed by amended Rule 11UA of the Rules.

Recommendations

- It is suggested that suitable amendment be made in the Rule 11UA to provide that the fair market value of the underlying assets for valuation of an unquoted equity share should only be adopted in cases of transactions resulting in change in control and management in the company. Further, to determine, “control’ or “ownership of the company”, precedence can be taken from prevalent practices/rules followed under the Act and may be appropriately provided for in the rules. It may be considered to exempt valuation of unquoted equity shares at FMV if the transferor held less than 25% of the shares.
- Provisions of section 50CA of the Act may not be made applicable to transfer of shares (other than quoted shares) of companies which are under resolution plan under the Insolvency and Bankruptcy Code, 2016 and such plan is approved. Similarly, section 56(2)(x) of the Act, interalia, may also not be made applicable on receipt of shares and securities of companies which are under resolution plan under the Insolvency and Bankruptcy Code, 2016 and such plan is approved.
- It is recommended that where the date of agreement for fixing the consideration for transfer of shares is different than actual transfer of shares, at the option of the taxpayer, in determining the applicability of section 50CA and section 56(2)(x) of the Act, Rule 11UA value prevailing on the date of agreement fixing the consideration be considered.
- Section 56(2)(x) of the Act should be amended so as not to apply to the issue/ allotment of new shares by a company, but only to transfer of shares, because the intent was always to bring within the tax net, transfer of shares for nil or inadequate consideration.
- It is recommended that the provisions of section 50CA of the Act should not be made applicable on transfer of unquoted shares between related parties or relatives (similar to exclusion provided in section 56(2)(x) in case of relatives).
- It is recommended that, in the definition of ‘quoted shares’, shares of foreign companies which are listed outside India be included and accordingly, provisions of section 50CA of the Act are not made applicable to foreign companies whose shares are listed outside India.
- Section 50CA of the Act may be amended to provide carve out for shares of foreign companies listed outside India.
- Instead of providing positive list of exempt transactions, the list should be formulated as a negative list, wherein only certain cases which are indicative of tax abuse practice are subjected to the anti-abuse provisions of section 56(2)(x) and section 50CA of the Act, leaving off the other transactions out of its application, akin to the negative list of transactions which were notified for the purposes of non-applicability of section 10(38) of the Act.
- The CBDT may exercise powers granted u/s. 50CA and s.56(2)(x) to prescribe the circumstances under which the said provisions will not apply to bonafide transactions.

This will become very crucial for business reorganisation arising in the aftermath of Covid-19 pandemic where many businesses will get restructured due to financial distress.

9.26 Issues relating to valuation of unquoted equity shares for the purpose of section 50CA and section 56(2)(x) of the Act

The Rules seek to determine the FMV of unquoted equity shares of the company by adopting the independent fair valuation of jewellery, artistic work, immovable property and shares and securities held by such company while all other assets and liabilities of such company would continue to be valued at book value.

Our recommendations on the valuation rules are set out below:

- The Rules do not envisage a scenario in cases of cross holdings amongst companies. Consider a situation where Company A and Company B hold shares in each other as "Investments" in their respective balance sheets and shares of Company A are subject matter of transfer. In this situation, as per the Rules, the FMV of shares of Company A will depend on FMV of shares of Company B and vice versa. As a result, there will be a continuous resilient loop in such cases. Suitable guidelines in this regard should be formulated.
- The aforesaid issue would also arise in cases of circular chain holdings. For instance, consider a situation where Company A holds shares in Company B which in turn holds shares in Company C which in turn holds shares in Company A. If shares of Company A are a subject matter of transfer, the valuation of shares of each company will be dependent on the other which will again result in a circular loop. Suitable guidelines in this regard should be formulated.
- There are several cases where shares of a company are sold in distress. In such cases, the book value of the company is significantly higher than the real economic value. In such cases, valuation of equity shares should, at the option of the taxpayer, be made at (a) book value as determined under these rules, or (b) FMV as determined under any internationally accepted valuation methodologies, whichever is lower. Similar option should also be provided to companies which are incurring persistent losses since, say, last 3 years. This approach can be implemented by enabling the Assessing Officer to adopt such lower value in cases where it is demonstrated that the value determined under the Rules is higher than the actual fair value. An advance determination of such value by the Assessing Officer may also be provided for.
- This section could also pose several practical challenges for shareholders (especially minority shareholders) desirous of transferring their shares – in terms of availability of audited accounts as on the valuation date, availability of details of immovable property/ arts/ jewellery, etc. and obtaining a valuation thereof.

  Given the same, an alternate manner of determining the FMV where such details are not provided to the shareholders should be provided for. Alternatively, a threshold limit could be provided for non-applicability of this section to minority shareholders.

- Furthermore, since the Rules are retroactively applicable from 1 April 2017, they may create unintended consequences for parties to the transaction, as also for persons liable to withhold tax or representative assesses who carry vicarious liability as they would have relied upon the extant valuation rules based on the book value for transactions already consummated post 1 April 2017. This would be contrary to the professed tax policy of the current Government of India of not introducing any retroactive amendment which creates higher tax burden. Thus, transactions which are already consummated prior to date of notification of new rules should continue to be governed under the erstwhile Rule 11UA.
- The Rules can possibly create conflict in respect of transactions which are covered by other provisions of the Act (say, transfer pricing), or in cases where the applicable regulatory provisions (FEMA, etc.) provide for differential FMV determination. Given the same, if the transfer price is in consonance with the price determined as per transfer pricing or other regulatory provisions, such price should be regarded as meeting the requirements of section 56(2)(x) and section 50CA of the Act.
- Contingent liabilities should be allowed to be reduced while calculating the FMV of shares since in any typical third party deal, there is a mark down for the contingent liabilities.
- Most of the manufacturing companies have land and building as their significant assets which are not separable from the business operations. In such cases, valuing the land and building based on their FMV may lead to a value which is significantly higher than the real economic value of the business. In such cases, it is recommended that land and building be valued at book value as per the prevailing Rule 11UA. However, for companies engaged in real estate activities, valuation ought to be done based on FMV as suggested in the Final rules.

9.27 Minimum Alternate Tax – Allow aggregate of brought forward business loss and unabsorbed depreciation

The companies who does not opt for the concessional tax regime will continue to be governed by the provisions of MAT. Presently, the amount of loss brought forward or unabsorbed depreciation whichever is less as per books of account is allowed as a deduction while computing book profit under section 115JB of Act. The said provision would adversely affect a company which has huge book losses and less unabsorbed depreciation as they will have to pay MAT despite having ample amount of book losses thereby affecting their cash flows. It is recommended that entire book loss brought forward, and unabsorbed depreciation brought forward should be allowed to be set-off from book profit for the purpose of MAT.

9.28 Ensure that new trusts are not deprived of registration in the first year of application under the new regime

Issues

- A trust which is formed after the new provision becomes effective, is required to make an application under s. 12A(1)(ac)(vi) which reads as under:

  "(vi) in any other case, at least one month prior to the commencement of the previous year relevant to the assessment year from which the said registration is sought

- Thereafter, such trusts are granted provisional registration for a period of 3 years automatically under s. 12AB(1)(c) which reads as under:

  "(c) where the application is made under sub-clause (vi) of the said clause, pass an order in writing provisionally registering the trust or institution for a period of three years from the assessment year from which the registration is sought"

Recommendation

- As per the plain reading of the aforesaid provisions for making an application and granting registration under the new regime, the new trust can get registration only from the next year immediately succeeding the year in which application is made and not from the same year in which application is made.
- For instance, a trust formed in January 2021 is required to make an application at least one month prior to the commencement of the previous year (i.e. FY 2021-22) relevant to the assessment year from which the said registration is sought. Therefore, the provisional registration will be granted to such trusts from next year and the trust will not be able to claim exemption under s. 11 to 13 of the ITA for FY 2020-21.
- The issue is more relevant for a trust which is formed in the last month of a financial year and hence will not be able to claim exemption even for the immediate next financial year.
- This does not appear to be the intention of the legislature. Therefore, it is recommended to remove such lacuna in the language and such trusts should be granted benefit of provisional registration (which is granted on automatic basis) from the year of formation or at least from the year in which application is made by new trust.

Section X

Personal Income Tax

10.1 Clause (vii) and (viia) sub-section (2) under Section 17

As per the earlier provision (sub-clause (vii) of Section 17(2)) of the Income-tax Act employer's contribution to superannuation fund, in excess of Rs.1.5 lacs was to be treated as perquisite, hence made taxable.

The above said clause has been amended by the Finance Act, 2020 wherein exempt contribution which an employer can make towards recognized Provident Fund (PF), National Pension scheme (NPS) and Superannuation Fund (hereinafter collectively referred to as 'employee welfare schemes') is capped at Rs. 7.5 lacs. The clause provides contribution to ‘employee welfare schemes’ if in excess of Rs. 7.5 lacs, the differential shall be taxed as perquisite in the hands of the employee.

Further, insertion of new sub-clause (viia) provides that interest/dividend accrued on any contribution to employee welfare schemes made by the employer, exceeding Rs. 7.5 lacs shall also be taxed as perquisite in the hands of the employees.

Issues

The issues emerging due to the aforesaid amendments are listed here-in-below:

- There is a challenge in identifying the interest relevant to the excess contribution from the total interest getting credited to an employee’s account. Interest accumulation is on the opening balance and monthly contributions on a cumulative basis, hence deriving interest accrued on excess contribution will vary for different companies as it will be based on assumptions and the Returns being generated by individual funds.
- Further PF and SAF interest rates are declared after the close of the financial year, hence it is not very clear as to how the same would be taken for salary TDS computation in the previous year.
- Income on NPS account is a notional gain on a year-on-year basis as there is change only in net asset value of the fund. It is not clear as to how income on NPS for employer’s contribution exceeding the specified limit will be taxed annually as no real income gets credited to the employees account.
- Employer has no control over income being generated by the Trust registered under the Income Tax Act. This calls for rules and timelines to be framed where information is to be shared by the Funds on timely basis with the employer facilitating deduction of accurate tax as per the Rules within the same financial year.
- If employer starts recovering TDS on estimated accrual it will complicate matter as the determination of income is ambiguous.
- Reasons why the provisions require a review

- The Explanatory Memorandum to Finance Bill 2020 provides the following rationale for the provision

  "Under the existing provisions of the Act, the contribution by the employer to the account of an employee in a recognized provident fund exceeding twelve per cent of salary is taxable. Further, the amount of any contribution to an approved superannuation fund by the employer exceeding one lakh fifty thousand rupees is treated as perquisite in the hands of the employee. Similarly, the assessee is allowed a deduction under National Pension Scheme (NPS) for the fourteen per cent. Of the salary contributed by the Central Government and ten per cent of the salary contributed by any other employer. However, there is no combined upper limit for the purpose of deduction on the amount of contribution made by the employer. This is giving undue benefit to employees earning high salary income. While an employee with low salary income is not able to let employer contribute a large part of his salary to all these three funds, employees with high salary income are able to design their salary package in a manner where a large part of their salary is paid by the employer in these three funds. Thus, this portion of salary does not suffer taxation at any point of time, since Exempt-Exempt-Exempt (EEE) regime is followed for these three funds. Thus, not having a combined upper cap is iniquitous and hence, not desirable."

- It may be noted that contributions to approved superannuation fund and NPS are not fully under EEE regime since the pension income received from such contributions are taxable.

* This results in double taxation of contribution in excess of Rs. 7.50 lakhs or interest/accrual thereon as also pension income. Provident fund contribution is fully taxable if withdrawn within a period of five years. This will also result in double taxation of contribution in excess of Rs. 7.50 lakhs or interest thereon and the withdrawal within five years.

  - In any case, the ceiling limit should not apply to employer's contributions to NPS since NPS was introduced as an alternative to PF or direct pension benefit from employer. NPS gives opportunity to employee to control the investment by selecting fund manager and investment pattern of his choice and thus become exposed to the investment risk on the fund. NPS is a modern scheme introduced in 2004 benchmarked with international standards. The Government has so far adopted a benign tax regime for NPS by providing for higher tax benefit on withdrawal. Initially, NPS was purely on EET basis and entire withdrawal was taxable. Subsequently, 40% of withdrawal was made exempt in 2016 which was enhanced to 60% by Finance (No.2) Act 2019. In 2017, even partial withdrawal upto 25% was made exempt. As a result of these measures, many employees in private sector have joined NPS. Limiting the contribution to Rs. 7.50 lakhs for all employees without making any distinction between existing and new employees creates tax uncertainty for the employees. It defeats the object of tax incentives so far provided by the Government to popularise the scheme. Minimum 40% of the corpus is received in the form of taxable pension and to that extent, it is under EET regime.

Recommendations

The concept of Exempt-Exempt-Exempt (EEE) for social security schemes such as PF, SAF and NPS is being diluted for the high-income group. This may discourage long term investment and may even be contradictory to the principles of good tax governance. It is therefore requested to review section 17(2)(vii) i.e. on taxing Employer contribution beyond Rs 7.5 Lakhs and interest accretion thereon u/s 17(2) (viia). It is submitted that contributions to approved superannuation fund and NPS be kept out of the scope of the provision considering that they are already under EET regime (albeit partially).

By dint of this amendment we may be upsetting the fundamental attractiveness of the retiral schemes in which citizens invest, as its importance needs no elaboration given lack of social security structure in our country.

In any case, appropriate clarificatory amendments are required to provide that once the excess contributions and interest/accrual thereon are taxed in the year of contribution/accrual, they shall not be taxable again in the year of withdrawal.

We plead that interest on excess contribution should not be made taxable in view of difficulties in computation thereof.

The employer should be relieved of the obligation to do salary TDS on the interest portion in view of the difficulties for the employer to get the information in timely manner. The employee may be cast responsibility to pay self-assessment tax thereon.

We submit, issues detailed above are critical, as for the first time the concept of EEE has undergone change.

10.2 Taxation of Employee Stock Option Plans for Migratory Employees - Section 17

Issue

- Section 17(2)(vi) of the Act, read with Rule 3 of the Rules deal with taxation of Employee Stock Option Plans (ESOPs). It is provided that the value of any specified security or sweat equity shares allotted or transferred, directly or indirectly, by the employer, or former employer, free of cost or at concessional rate shall be taxable as perquisite in the hands of the employee. For this purpose, the value of any specified security or sweat equity shares shall be the fair market value of the specified security or sweat equity shares, as the case may be, on the date on which the option is exercised by the taxpayer, as reduced by the amount actually paid by, or recovered from, the taxpayer in respect of such security or shares.

Issues

- Notwithstanding the above recommendation, 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.

- There was a specific clarification on proportionate taxability of benefits under the erstwhile FBT regime, 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 taxation regime from 1st April 2009.
- Considering the various judicial precedents on the issue only the proportionate benefit of ESOP pertaining to the services rendered by taxpayer in India should be taxable in India and not the entire benefit.

Recommendation

- A specific clarification should be inserted with respect to taxability of only proportionate ESOP benefit based on residential status of the individual, where an employee was based in India for only a part of the period between grant and vesting.

10.3 Introduce concept of "fair rental value" for determining perquisite value in case of company owned accommodation provided to its employees

As per Section 17(2) of the Income Tax Act, 1961, "Perquisite" includes value of rent-free accommodation provided to an assessee by his employer. The methodology for computing its perquisite value as prescribed under Rule 3(1) of Income Tax Rules, is tabulated below:

Basis of Valuation of Perquisites - Rent Free Accommodation

Population of City As per 2001 Census	Where Accommodation is owned by Employer	Where Accommodation is taken on Lease by Employer
Exceeding 25 lakhs Exceeding 10 lalhs but below 25 lakhs Any Other	15% of Salary 10% of Salary 7.5% of Salary	Lease Rent Paid or Payable by Employer (or) 15% of Salary, whichever is lower *(less)* rent, if any, paid by the employee

'Salary' for the above purpose includes: Pay, Allowances, Bonus or Commission or any other monetary payment but does not include DA, Employer's contribution to PF, allowances exempt from tax and value of perquisites

Issues

The method of determination of perquisite value in respect of company owned accommodation suffers from various inequities, as summarised below:

- Firstly, the perquisite value and the consequent tax implication on a company owned accommodation is not linked to the rental value of the said property; instead it is linked to the Salary earned by the employee, which is not a fair benchmark to determine the perquisite value of such accommodation.
- Secondly, such perquisite value in case of company owned accommodation is significantly more than on an accommodation taken on lease by an Employer. This could be best illustrated by way of an example as below:
- Let us assume that an Employer owns a Flat in a residential complex in Mumbai which is offered to one of its employees (say 'X'); let us also assume, the Employer takes on lease another but a similar flat in the same residential complex at a rental of, say, Rs.3 lakhs

per month and offers it to one other employee (say 'Y'). Then, the perquisite value of the accommodation provided to X and Y & related tax15 would be computed as below:

Scenario 1

Amount / Rs Lakhs	**X**	**Y**	**Tax Differential**
Annual Salary	400	400	
Annual Lease Rent	-	36	
Methodology for comptuing Perqusiite Value	15% of Salary	Lease Rent Paid (or) 15% of Salary, whichever is lower	
Perquisite Value of Rent-free Accommodation	60	36	
Income Tax @ 39% [i.e. 30% + SC @ 25% + Cess @ 4%]	23.4	14.0	**9.4**

It could be observed from the above table that the tax impact on X staying in a company owned accommodation is much higher than for Y who is staying on a company leased accommodation, by Rs.9.4 lakhs – though both are earning same salary, and both are staying in similar type of accommodation

- Secondly, where the salary of employees increases (considering inflation, performance of the company, employee etc.) equally, in respect of the employee staying in the same company owned flat, the perquisite value and related tax implication will be much more as compared to the other employee staying in the accommodation taken on lease by the employer – see illustration below

Scenario 2

Amount / Rs Lakhs	**X**	**Y**	**Tax Differential**
Annual Salary	450	450	
Annual Lease Rent	-	36	
Methodology for comptuing Perqusiite Value	15% of Salary	Lease Rent Paid (or) 15% of Salary, whichever is lower	
Perquisite Value of Rent-free Accommodation	68	36	
Income Tax @ 39% [i.e. 30% + SC @ 25% + Cess @ 4%]	26.3	14.0	**12.3**

[15] *For simplicity sake, Tax rate has been applied on the total salary without factoring in slab benefits – i.e. Up to Rs.2.5 lakhs: Nil; 2.5 – 5 L: 5%. 5 – 10L: 20% & above Rs.10 L: 30%*

As illustrated above, the tax implication on X staying in company owned accommodation will be significantly adverse [i.e. by Rs.12.3 lakhs], despite X continuing to stay in the same flat. Whereas in case of Y, where the accommodation is taken on lease by the employer, the perquisite value is fair and stable, since it is linked to lease rental value.

In the above illustration, if the Total Salary of X (employee staying in company owned accommodation) crosses the slab of Rs.5 crores (thereby attracting higher surcharge) due to his/her relatively superior performance compared to Y, then the perquisite value of rent-free accommodation & related tax implication would be as below:

Scenario 3

Amount / Rs Lakhs	**X**	**Y**	**Tax Differential**
Annual Salary	525	475	
Annual Lease Rent	-	36	
Methodology for comptuing Perqusiite Value	15% of Salary	Lease Rent Paid (or) 15% of Salary, whichever is lower	
Perquisite Value of Rent-free Accommodation	79	36	
Income Tax @ 42.74% [i.e. 30% + SC @ 37% + Cess @ 4%] / 39%	33.7	14.0	**19.6**

It may be noted that the tax paid by Y remains the same in all the 3 scenarios, reason being the perquisite of the accommodation provided to him/her is linked to the fair rental value of the said property. On the other hand, the tax implication on X changes adversely with every increase in salary, even though he/she stays in the same accommodation. It may be noted that, neither the employer nor the employee change the accommodation frequently or every time his/her Salary is increased. So, increase in perquisite valuation of such accommodation & related tax impact happens mechanically, without any correlation to the quality/size of accommodation provided to employees.

And the tax impact becomes worse if his/her salary crosses the slab of Rs.5 crs attracting higher surcharge[16] – **this increase in rate would have adverse impact on his total salary, resulting in a situation where his/her take home salary after tax could be even lower than Y, despite X's performance rating being superior compared to Y**

Further, for a similar company owned accommodation, employees with different salaries will have different perquisite value. To illustrate, assuming the Employer owns 2 similar flats in a residential complex offered to two of its employees, the tax implication would be adverse for the employee whose salary is more than the other one, as illustrated below:

[16] *Surcharge on Income Tax stands at 10% for Income between Rs.50 L – 1 cr; 15% for Rs.1 cr – 2 cr, 25% for Rs.2 cr – 5 cr and 37% for Income above Rs.5 crores.*

Scenario 4

Amount / Rs Lakhs	**X**	**Y**	**Tax Differential**
Annual Salary	400	300	
Annual Lease Rent	-	-	
Methodology for comptuing Perqusiite Value	15% of Salary	Lease Rent Paid (or) 15% of Salary, whichever is lower	
Perquisite Value of Rent-free Accommodation	60	45	
Income Tax @ 39% [i.e. 30% + SC @ 25% + Cess @ 4%]	23.4	17.6	**5.9**

It can be appreciated from the above illustrations, irrespective of the size or quality of company owned accommodation, the perquisite value and the consequent tax implication on the employees keeps increasing significantly, since under the present law, it is getting determined as a percentage of salary, without any correlation to the fair rental value of the said accommodation.

Implications

1) Retention of skilled manpower is a critical requirement for a company to be successful on a sustainable basis. One of the motivating tools adopted by corporates is to provide a good quality residential accommodation (typically owned & maintained by corporates) and related facilities to its employees & their families. However, the perquisite valuation methodology currently prescribed under the Income Tax Act, acts as a deterrent to employees from willing to accept and stay in company owned accommodation.

2) Secondly, employees exhibiting superior performance and staying in company owned accommodation, are getting demotivated since their take home salary after tax, turns out to be lower than a moderate performing employee due to following reasons:

   (i) higher tax outflow towards perquisite value of accommodation which is linked to their higher salary vis-à-vis a lower salaried employee, even though both are staying in similar type of company owned accommodation;

   (ii) where the superior performer's salary crosses the income slab [say above Rs.2 crores or above Rs.5 crores] due to the perquisite valuation of their accommodation, then their tax outflow will be even higher [due to higher surcharge impact] compared to another employee staying in a similar accommodation, but earning below the slab (due to relatively lower performance) and so paying lesser tax.

3) The aforesaid inequitable treatment also discourages corporates from investing in infrastructure, including residential projects, across the country. It may be noticed that for this very reason, several corporates have been disposing of their residential

properties across the country. At a time when the economy needs investments, it is submitted that the Govt. amends the perquisite valuation methodology for company owned accommodation such that corporates are incentivized to invest in the real estate sector (which is also a high employment intensive sector of the economy).

Recommendation

1) It is suggested that in case of company owned accommodation, the concept of "fair rental value" be introduced to ensure that right amount of perquisite is determined for tax purposes. "*Fair rental value*" for this purpose should be defined as the rent which a similar accommodation would realize in the same locality; where fair rental value is not ascertainable, then the municipal valuation should be considered for determining the perquisite value.

   The concept of fair rental value is very much well recognised while computing Income under the head House property and the same can also be brought in while computing the perquisite value in case of company owned accommodation.

2) Towards this, Sections 17(2)(a)(i) and 17(2)(c)(i) together with Rule 3(1) Table I – Clause 2(a) be deleted. Instead, Section 17(2)(a)(ii) and 17(2)(c)(ii) and Rule 3(1) Table I – Clause 2(b) be amended appropriately to include company owned accommodation as well, such that the perquisite valuation of such accommodation be based on the fair rental payable for such accommodation and where fair rental is not determinable, then the perquisite valuation of such accommodation be determined based on the municipal valuation – as is being followed for determining Income from House Property under Section 23(1) of the Income Tax Act.

10.4 Increase in limit of Standard Deduction

Issues

- The Finance Act, 2018 has introduced a standard deduction from salary income upto Rs. 40,000 in lieu of reimbursement of medical expenses and transport allowance. Further, the benefit of additional deduction of Rs. 5800 is also reduced by the increase in cess rate from 3% to 4%. Standard deduction has been further increased to Rs. 50000 by the Finance Act, 2019.
- Further, basic exemption limit has also not been increased which was much expected by the salaried class.

Recommendations

- The standard deduction for salaried employees should be reinstated to at least Rs. 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. Also, particularly on ground of increasing trend of 'Work from Home' culture during COVID-19 pandemic period where employee incurs higher work related personal expenditure (like higher electricity, air conditioning, food, etc.)

- This should also reduce the disparity between salaried and business class with only the latter being eligible for deduction for expenses incurred by them for earning their income.
- Alternatively, the exemption towards reimbursement of medical expenses and transport allowance should continue in addition to standard deduction.

10.5 Provision of Treaty benefits while calculating TDS under Section 192

Issues

- Under the current tax regime, there is no provision under the Act which enables an employer to consider admissible benefits under the respective Double Taxation Avoidance Agreements (e.g. credit for taxes paid in another country/ treaty exclusions of income etc.), while computing tax to be deducted under Section 192 at the time of payment of salaries to employees. Further, the foreign tax credit rules notified by the CBDT in June 2016 also does not contain explicit provision for providing credit for taxes paid in another country by the employer at the time of deduction of tax on salary payments.
- This creates cash flow issues for the expatriates who are initially subject to deduction of tax by their employers and then are required to claim large refunds on account of treaty benefits at the time of filing their return of income. Many of these employees complete their assignments and leave India prior to obtaining their tax refunds which also creates hardships with respect to receiving back the refund amounts.
- Further, Authority for Advance Rulings has in the recent past held that Foreign Tax Credit may be considered at the withholding stage by the Indian employer while determining withholding tax on salary income for employees qualifying as Resident and Ordinary Resident in India.

Recommendation

Since the credit is otherwise admissible in terms of Section 90/91 of the Act, a suitable amendment may be incorporated in Section 192 of the Act providing for the employer to consider such credits/exclusions at the time of deducting taxes. This amendment would also be in line with the existing provisions under section 234A, 234B and 234C of the Act which provides for claiming relief under section 90/ 90A/ 91 of the Act at the time of calculating the tax in default on which interest is to be calculated.

10.6 Threshold Limit under Section 80C of the Act

Issues

- Over the years, investments made in various avenues available under Section 80C of the Act have helped the Government to raise funds as well as the individuals to save tax.
- However, with too many investment/ expenditures clubbed into the existing overall limit of Rs. 150,000 (including contribution to pension funds under Section 80CCC, pension scheme under Section 80CCD of the Act), individuals sometimes are discouraged from making further investments.

Recommendations

- There must be a clear distinction between long-term and short-term savings. So far there has not been any significant support in tax policy to actively encourage “long-term savings” which is very much needed. Life insurance and pensions are the main segments of the financial services that address the needs of individuals in the long-term. It would be equally desirable to have many more such tax-exempt investment avenues to mobilize funds for infrastructural and overall economic development. Therefore, the Government may consider separate exemption limits for such important avenues.
- Further, the Government may look at increasing the overall deduction limit to at least Rs. 300,000 to boost further investment and increase tax savings for the individual.

10.7 Provide marginal relief if total income of resident individual taxpayer crosses Rs. 5 lakhs threshold by a small margin

To alleviate the difficulty for small taxpayers, it is recommended that the concept of marginal relief should be introduced for small taxpayers where their total income marginally exceeds the threshold of Rs. 5 lakhs such that tax liability does not exceed the incremental income beyond Rs. 5 lakhs.

10.8 Simplify procedure for submission of Form 12BB

Rule 26C of the Rules (which prescribes the form and manner of collecting evidences and proofs of prescribed claims from employees while estimating salary income under section 192 of the Act) may be amended to enable furnishing of Form 12BB and supporting evidences to employer either with digital signature or through any electronic functionality created by employer which has an employee-authentication process.

INDIRECT TAXES

A. POLICY AND PROCEDURAL ASPECTS – CUSTOMS AND EXCISE

1. Provide credit of GST against excise duty on petroleum products

Existing Law

Currently, petroleum crude, motor spirit (petrol), high speed diesel, natural gas and aviation turbine fuel is out of the purview of GST. Accordingly, input tax credit of GST paid on procurements is not allowed against the output tax liability to the supplier of the said products and is an additional cost for the producers of oil and gas.

Issue

Non-inclusion of petroleum products under GST regime and levy of GST on inputs has led to high incidence of tax on the suppliers of petroleum products.

Recommendation

Until introduction of GST on petroleum products, it is recommended that producers of petroleum and natural gas should be allowed to claim credit for GST on all inputs, input services and capital goods being paid by them to be allowed to be set-off against output excise duty and VAT (due deliberations may be carried out in the GST Council meeting regarding allowability against VAT) on these products. Appropriate suitable amendment may be carried out in the CENVAT Rules and VAT laws.

Justification

This will ensure that credit for input tax is provided and there are no stranded costs for the suppliers of petroleum products.

2. Synchronise customs data related to exports made to SEZ with EDI database

Existing Position

As per current system, Customs department in SEZ is maintaining online data separately (not synchronized with EDI port system) and due to which the supplies to SEZ (Deemed Exports) are not getting updated in EDI system.

Issue

For claiming drawback against the exports made to SEZ Units, manual application along with all proof of exports such as Shipping Bill, Invoice, Bill of Export etc. are required to be submitted to jurisdictional Customs officials which requires additional efforts and involves transactional costs.

Recommendation

It is recommended that the SEZ customs data is synchronized with EDI database so that the process can be made paperless. This will save transaction costs to exporter and aid government drive for ease of doing business.

3. Automate updation of shipping bill data in banks /Customs server to DGFT server

Existing Position

Banks while issuing bank realization certificate (BRC), are updating the details of shipping bill manually.

Issue

If the bank officials make any data entry error while updating the details, the exports are facing problems in claiming export benefits like MEIS as the Shipping Bill details does not appear in the DGFT portal. Further in some cases errors are made by Custom department in uploading shipping bills in DGFT portal.

Recommendation

It is recommended that the above-mentioned processes are automated so that clerical mistakes are avoided for seamless process –

a. Shipping Bill data is picked by Bank from customs database instead of feeding the data manually

b. Data transfer of Shipping Bills from Customs server to DGFT server is made automatic

4. Minimise documentation submission - Stuffing of containers for export under self-sealing procedure

Existing Position

Over a period of time CBIC has relaxed the procedural aspects pertaining to permission for stuffing of export containers under self- sealing mechanism including removal of supervision by customs authority, which is a progressive step taken by the Board. However, the ongoing pandemic has created new challenges to the business which requires few more procedural reforms in order to address the operational issues such as connectivity whether through courier or in any other form. As part of the self- sealing procedure, department has been insisting for submission of multiple documents from all the exporters irrespective of whether the concerned exporter is a status holder or not. The companies are required to apply for self-sealing for every new premises with the Jurisdictional Authority. The list of documents is shared by the Jurisdictional Authority upon application by the Exporter. The multitude of documents to be submitted includes, GSTR-3B for last 2 Years, GSTR-1 for a Quarter, Details of Directors, PAN of the Company, Directors, Certificate of Incorporation, Bank statement for last 2 years etc.

Issue

The list of documents sought are not uniform across jurisdictional authorities. Hence, there are multiple correspondence between the Exporter and authorities for submission and verification of requisite data. Further, the process of application, submission of documents, its verification and approval require physical contact. Most of such information sought from the exporter are available with DGFT/Departments of CBIC. Hence, submission of the above

is a redundant activity, along with each application seeking permission for new units. This causes operational difficulties and increases the time taken for Export.

Recommendation

It is recommended that, appropriate clarification/circular be issued so as to allow the 4 star and above status holders as per Foreign Trade Policy to

- Submit minimum standardized documentation alone viz., Agreement with the Warehouse Service Provider/ Manufacturer, Address Proof of the Premises, Declaration only in respect of the additional premises while seeking approval and a centralised repository for documentation which is common across additional premises to avoid its resubmission;
- Submission of the application and supporting documentation through an e-enabled facility in an on-line portal in order to fast forward the process of application submission and its processing by the department in a time bound manner to ensure transparency and greater flexibility to the process.

5. Permit Importers with AEO Status to Carry Labelling Post Customs Clearance

Existing Law

Legal Metrology Act, 2009 requires all consumer products to be compliant to the regulations at the time of import. Directorate General of Foreign Trade (DGFT) has published this under the Foreign Trade Policy and accordingly the customs authorities have provided provisions through Notifications permitting importers to carry out the labelling in bonded warehouse if foreign supplier is not able to provide consumer packs with the labels.

Issue

It may be noted that under the erstwhile indirect tax regime, MRP had a major bearing on the value of certain specified goods imported into India for the purposes of calculation of customs duty. Accordingly, customs authorities were required to validate the MRP. Further, under the GST regime, for the purposes of Integrated Goods and Services Tax ('IGST') which is being computed on the transaction value, MRP except in case of certain goods like footwear does not have any relevance. Accordingly, the procedure of labelling to be carried out by the importers in the bonded warehouse only increases unwarranted compliance burden and cost for the importers without any revenue implications for the Government.

Recommendation

It is recommended that the importers with AEO Status be permitted to carry out the labelling post clearance from customs and in their own warehouses which are registered with the Legal Metrology Department.

Justification

The permission to label post customs clearance will entail the following benefits:

- This will reduce the burden of documentation on both importer and customs authorities as the importers would need to file only one Home Consumption Bill of Entry (BoE) instead of two (Warehousing Bill of Entry and Ex-Bond Bill of Entry) currently.

- There are several additional bonds that need to be debited and cancelled, etc. which can be completely avoided.
- Importers can save costs of double handling goods in the bonded warehouse as well as costs of running a bonded warehouse operation. This would be a significant cost saving that will benefit consumers also.
- The warehouses would be registered under Legal Metrology Act, 2009 their officers can oversee compliances in a better way through site visits etc.
- Moreover, being AEO importers, the customs can also oversee compliances as On-Site Post Audit instead of real time that delays overall process.

6. Allow acceptance of certificate of origin in digital mode for clearing of import consignments by Indian Customs

Existing Position

Certificate of Origin is an instrument which establishes evidence on origin of goods imported into any country. These certificates are essential for importers to prove where their goods come from and therefore stake their claim to whatever benefits goods of foreign origin may be eligible for in India. There are two categories of Certificate of Origin – (1) Preferential and (2) non-Preferential.

Issue

Preferential arrangement/scheme under which India is giving tariff preferences for its Imports from certain countries. Indian Customs have been insisting for Certificate of Origin in Original from Importers which has been causing enormous difficulties to the trade, especially due to the prevailing Covid-19 environment since the same has to be obtained from foreign vendor through courier.

Recommendation

Indian Customs has been insisting for Certificate of Origin in Original from Importers which has been causing enormous difficulties to the trade, especially due to the prevailing Covid-19 environment. Obtaining the same from foreign vendors include courier and physical logistics related logistics. It is recommended to allow acceptance of certificate of origin in digital mode for clearing of import consignments by Indian Customs.

7. Provide procedure for time bound re-assessment of bill of entry with incorrect/excess debit to the bond

Existing Position

Section 18 of the Customs Act provides for the circumstances under which the proper officer can assess the imported goods provisionally. Customs (Provisional Duty Assessment) Regulations 2011 provides that where the proper officer on account of any of the grounds specified in sub-section (1) of section 18 of the said Act, is not able to verify the self-assessment or make re-assessment of the duty on the imported goods or the export goods, as the case may be, he shall make an estimate of the duty to be levied (hereinafter referred

to as the provisional duty) and Importer shall provide for the Provisional Duty (PD) Bond for such amount to enable the proper office to assess the duty on goods provisionally and release the Cargo. Upon submission of such PD bond by the Importer, the assessment is completed by debiting the value of duty for the subjected import to the bond value.

Issue

The above provision is a relief to the importer, there are times when the duty amount is incorrectly/excess debited to the bond as compared to provisionally assessed value. In such cases, while there is an option of recalling such incorrectly assessed bill of entry and re-assess/re-debit the correct bond value, the amount of time taken for such procedural regularisation is high resulting in severe financial hardship on importer in the form of demurrage and detention charges due to delay in release of cargo. This delay results in severe financial hardship on importer in the form of demurrage and detention charges due to delay in release of cargo.

Recommendation

In the backdrop of Ease of Doing Business, it is recommended that re-assessment of bill of entry with incorrect/excess debit to the bond should be done in a time bound manner and multiple layers of approvals may be pruned to speed the entire process.

Due to rapid fluctuation in commodity prices further accentuated by shipping disruptions, the import prices of certain inputs can vary from shipment-to-shipment by a large measure. This can lead to delays during the process of faceless assessment which relies mainly on time series price movements. It is recommended that this may be addressed by an advisory or customs department circular.

8. Do away with the requirement of registration of the licence for export incentives with the Customs Department

Existing Position

Several initiatives have been taken by the Government of India in the area of automation, of various processes thereby facilitating ease of doing business. This also includes automating certain processes involved with regard to export incentives licences under FTP which have enabled expeditious issue of export incentive licences.

a. Online application for licenses on the DGFT website which is then validated through the digital certificates of the exporter.
b. While filing the application the linking of the Shipping Bills and the BRCs are also done online by the exporters.
c. The licences are then issued online.

Issue

As per current practice, after obtaining such licence from DGFT, the licence holder is required to get the licence registered with the Customs Department which involves significant efforts and multiple follow ups.

Recommendation

As the details of the licence are already getting transferred from DGFT server to Customs server, it is recommended that the formality of registration of the licence with the Customs is done away. This will eliminate the transaction cost involved in registration and also help in saving time of importers as well as Customs officials.

9. Automate the process of uploading of responses to Queries Raised

Existing Position

At the time of filing the Bill of Entry, all prescribed documents are uploaded in e-Sanchit. As per the current practice, uploading the query documents are done manually at the service centre.

Issue

This process completely defeats the purpose of online documentation and also results in delays as the service center works only for a specific time period in a day.

Recommendation

It is recommended that an online workflow system be introduced enabling the Trade to respond to the queries online itself.

10. Remove the process of Physical Signature of Preventive Officer on Gate Passes for Import Clearances

Existing Position

CBIC has launched electronic delivery of Gate Passes to customs brokers and importers with an aim to further simplify import clearance process by reducing human interface and help tackle the scourge of Covid-19.

Issue

These Gate Passes are digitally signed by the Preventive Officer and are supposed to be used for physical exit of the imported goods from the customs area. However, on the ground, the Customs Department insists on manual signature from the Preventive Officer even though the Gate Pass is digitally signed. This creates significant delays in clearance under the current circumstances where the working hours of the Preventive Officer are restricted due to COVID-19.

Recommendation

It is recommended that necessary instructions be issued by Customs for clearing consignments with digitally signed Gate Passes itself instead of insisting on manual signatures from Preventive Officer.

11. Align tariff codes to a digit ten structure

Existing Law

India has eight-digit uniform codes known as "Harmonised System of Nomenclature" that classifies more than 5000 products and is accepted worldwide. There was a recent DGFT Public notice seeking inputs from importers to clarify what separate tariff heading they want to be introduced in the ITC HS Tariff book. There were also some comments stating that there is an intention to put all classification of the residual category "Others" into restricted category of imports, which will require permits from the DGFT prior to import.

We appreciate the initiative taken by the Government to review the ITC HS tariff codes as there are no separate tariff codes for specific category of goods being imported forcing importers to rely on residual category "Others" in many cases.

Issue

Other countries have adopted a ten-digit tariff code structure as opposed to an eight-digit structure in India. This gives the authorities greater flexibility to regulate imports of goods into the country as specific tariff codes can flag compliance checks. For example, ITC HS 94049011 covers Quilts filled with feathers or down and the next available tariff code is 94949019 as Other. This means if an importer brings in Quilt made of artificial fibre then they will not have any option other than to classify the article under "Others" tariff code. Issues over identification of correct classification only results in delays, disputes and additional cost and increase of lead time for clearance of such articles.

Recommendation

It is recommended that the Government should consider aligning our tariff codes with that of other countries using ten-digit codes.

Justification

This will bring in more transparency in the trade and give importers the chance to use more appropriate tariff codes and avoid repeated disputes with the customs authorities on classification related issues.

12. QCO 2020 on Toys - Permit AEO importers to get sampling done from container after receipt at their warehouse for sending to labs under importer self-declaration

Existing Law

India has published its own Standards for articles from time to time. Government is working on implementing more standards under QCO 2020. There has been a recent shift in the verification of compliance to the standards from Manufacturer Declaration to Local testing. Till November 2019, all importers of Toys had to get a manufacturers declaration that the toys being shipped are compliant to the relevant Indian standards and based on the declaration and test reports the Customs Officer would release the cargo. Post November 2019 DGFT prescribed changes in import regulations which prescribes that the customs authorities would draw samples and send it to Local labs for testing. For each article of toy imported, the importers draw samples and hand it over to the customs officer for sealing

and allocating the lab for testing. Once the lab has been allocated the samples are sent through post to the labs which does not have any traceability.

Issue

Due to the above procedure, the importers have to rely on calling the labs to confirm receipt and status of testing. These labs are not all located in the city of import and can be sent to any lab in India making it very challenging. Further, there are no provisions like in case of textile import where a test report of an article has validity for six months basis which same article is permitted release during that period.

Recommendation

It is recommended as below:-

- Government to first develop test labs infrastructure near major ports of India.
- Implement such changes only after the necessary infrastructure is in place.
- Permit AEO importers to get sampling done from container after receipt at their warehouse for sending to labs under importer self-declaration as existing. This will reduce handling at port.
- Permit future import in the following six months without testing based on Previous Test report.
- Integrate this through ICEGATE like other PGA's to secure verification by the authorities.

Justification

This will improve the Risk Management System (RMS) facilitation and reduce handling of cargo at port that leads to damages and delays.

13. Review Animal Quarantine Regulations

Existing law

In around Feb 2019, there were changes in the customs procedures where certain tariff codes were identified between the Animal Quarantine (AQ) and Customs Authorities which will require NOC from the Animal Quarantine Authorities before customs release. This meant that importers would need to draw samples of each article in each container imported under those tariff codes and take them to the Animal Quarantine office instead of the officer visiting the port /CFCs to get a NOC from the AQ office and produce it to the Customs Authorities to get release. In addition, the AQ officer will tear the product to verify the filling inside the product is indeed not animal origin feather.

Issue

This ruins the product for sale and needs to be scrapped. There is also no provision under the procedure to accept self-declaration or treat previous release of the same article as reason for AQ/Customs authorities to release without sampling.

Recommendation

We refer to the example of classification of Quilts for this case. ITC HS 94049011 covers Quilts filled with feathers or down. In case an importer brings in quilts of manmade or non-animal origin quilt they will need to be classified under the next available tariff code is 94949019 as Other. The customs authorities should remove the tariff codes that do not specifically cover Animal Origin articles for release from AQ dept. They can instead ask importers to create a file with composition of their articles classified under these exempted tariff codes and do random inspection. The inspection also should be done by the AQ office at the Container yard and samples need not be taken out of the yard. This will further simplify the process and reduce lead times. Alternatively, importers with AEO status should be permitted to take containers to their warehouses and audit this post clearance and impose penalties if they have been found to be misusing the benefits.

Justification

This will reduce damages, corruption, lead time and costs and will also encourage importers to go for AEO certification.

B. TARIFF RELATED ASPECTS - RESCIND OUTDATED NOTIFICATIONS

This is with reference to the review exercise of Customs Duty exemptions being carried by Central Board of Indirect Taxes and Customs ('CBIC'). Our suggestions in this regard are given below for consideration of the Government: -

Serial Number 167 (List 4 – Item No. 43) of Notification No 50/2017 - Customs

Goserlin Acetate

Background and clinical experience

i. Goserelin (D-Ser(But)6Azgly10 LHRH) is a synthetic analogue of naturally occurring luteinising-hormone releasing hormone (LHRH). On chronic administration Goserelin results in inhibition of pituitary luteinising hormone secretion leading to a fall in serum testosterone concentrations in males. In men by around 21 days after the first Implant injection, testosterone concentrations have fallen to within the castrate range and remain suppressed with treatment every 12 weeks.

ii. Goserelin acetate 10.8 mg is approved by O/o CDSCO on 13th May 2004 for the treatment of prostate cancer suitable for hormonal manipulation.

iii. Goserelin acetate has been approved for endometriosis and thinning of endometrium outer layer (IVF) or for treatment of infertility issues caused by endometriosis.

Current Global Regulatory Status

As on May 2021, regulatory approval has been received for Goserelin acetate in over 118 countries worldwide O/o DCGI has Approved Goserelin acetate for the below mentioned Indications.

Goserelin is indicated in:

- The management of prostate cancer suitable for hormonal manipulation.

Stage B2-C Prostatic Carcinoma

Goserelin is indicated for use in combination with flutamide for the management of locally confined Stage T2b-T4 (Stage B2-C) carcinoma of the prostate. Treatment with GOSERELIN and flutamide should start 8 weeks prior to initiating radiation therapy and continue during radiation therapy.

Prostatic Carcinoma

Goserelin is indicated in the palliative treatment of advanced carcinoma of the prostate.

In controlled studies of patients with advanced prostatic cancer comparing Goserelin 3.6 mg to orchiectomy, the long-term endocrine responses and objective responses were similar between the two treatment arms. Additionally, duration of survival was similar between the two treatment arms in a major comparative trial.

In general terms Goserelin Acetate is the only LHRH molecule whose 10.8mg SKU has survival rate of 10 years as per the latest scientific data available. While 3.6mg SKU has the maximum scientific data in the treatment of endometriosis. Further, Goserelin Acetate being sold in a pre-filled syringe form results is very less possibility of error in drug dosing. Given the above, the above drug profile of the goserelin, it has been given the status of life saving drugs by the office of Drugs Controller General of India.

Existing exemption granted to Goserelin Acetate be retained considering the fact that it still remain categorized as a life-savings drugs and would lead to improvement in better patient outcomes with continuing access to affordability.

Serial Number 166 and 167 of customs notification no. 50/2017

Several of products (enclosed in the table below) would be impacted by removal of the customs exemptions under this notification and would lead to an increase in their price. This in turn, would affect the access of the patients to these important medicines, including life-saving medicines, and adversely impact the Government of India's commitment of making available these and other life-saving medicines to the patient at the lowest price.

S. No.	Drug/Molecule	Serial No.	Concessional Rate of Duty as per the notification	Unmet medical need – Justification for custom duty exemption
1.	Pneumococcal Polysaccharide Vaccine	166	5%	Preventive vaccine for pneumococcal diseases (caused by vaccine-serotypes) which have high burden of disease and responsible for hospitalizations and deaths among children and high-risk adults in India. Hence, Vaccine is required to made available in affordable price

				to the large population.
2.	Varenciline tartrate	166	5%	Smoking is one of the leading cause of lung cancer. And with increasing adoption of western culture the incidence rate of smoking is on rising curve. At present, Vareniciline this is the important therapeutic treatment for smoking cessation. Access and compliance to the treatment is critical to achieve maximum benefit with the therapy.
3.	Tranexamic Acid	167	0%	Bleeding is an important complication during and after surgery. This drug can help arrest bleeding induced complications and affordable availability of tranexamic acid is critical for maximum benefit to patients.
4.	Suntinib Malate	166	5%	RCC is most common kidney cancer. Sunitinib Malate is used in the treatment of advanced renal cell carcinoma and have median overall survival of 26.4 months v/s Interferon alpha.
5.	Clindamycin	166	5%	Clindamycin is an antibiotic used to treat susceptible gram positive aerobic and anaerobic organisms causing upper/lower respiratory tract infections, skin & soft tissue infections, gynecological infections and intra-abdominal infections. Clindamycin is an effective anti-infective in managing several serious infections caused by susceptible organisms.
6.	Anti-human lymophocyte immunoglobulin IV	167	0%	One of the commonly used drug for moderate to severe aplastic anemia who are unsuitable for bone marrow transplant.
7.	Low molecular weight heparin	166	5%	Dalteparin is frequently used to prevent the clotting related complications and is useful in COVID patients to prevent thrombotic complications. Hence, wider availability is essential.
8.	Somatropin	166	5%	Somatropin is indicated for the treatment rare growth disorders. if treatment of these growth disorders started early at appropriate time, it can help children with growth disorders to achieve normal height , therefore wider availability of somatropin for management of rare growth disorders at affordable prices is in best interest of rare growth disorder patient

FICCI

				and critical for treatment outcome.
9.	Epirubicin	167	0%	Anticancer drug used to treat multiple oncology conditions hence wider and affordable therapeutic option is key for Indian patients.
10.	Cytosine Arabinoside (Cytarabine)	166	5%	Anticancer drug used to treat multiple oncology conditions hence wider and affordable therapeutic option is key for Indian patients.
11.	Anti-Haemophilic Factor Concentrate (VIII and IX)	167	0%	Coagulation factors VIII and IX are used for the treatment Haemophilia A and Hemophilia B respectively which are rare bleeding disorders hence wider availability of treatment options is critical for continuation of treatment and maximum treatment benefits.
12.	Idarubicine	167	0%	Anticancer drug used to treat multiple oncology conditions hence wider and affordable therapeutic option is key for Indian patients.
13.	Latanoprost	166	5%	Used to manage the glaucoma which can lead to blindness for not attended in timely manner, can help reduce intraocular pressure and hence can reduce complications induced by glaucoma hence wider availability is key.
14.	Anidulafungin	166	5%	Echinocandin antifungal used to manage invasive candidiasis/candidemia and wider availability can help managing this fungal infection which has shown an increasing trend in hospitalized COVID patients hence continued affordable availability is crucial.
15.	Anti-Haemophilic Factor Concentrate (VIII and IX)	167	0%	Coagulation factors VIII and IX are used for the treatment Haemophilia A and Hemophilia B respectively which are rare bleeding disorders hence wider availability of treatment options is critical for continuation of treatment and maximum treatment benefits.
16.	Daunorubicin	166	5%	Anticancer drug used to treat multiple oncology conditions hence wider and affordable therapeutic option is key for Indian patients.
17.	Contraceptives	217	0%	The wider and affordable availability of contraceptives is effective way of controlling the unplanned pregnancies and its

				complications. Wider use of contraceptives is promoted by Government of India in national programs related to Maternal and child health.

It is accordingly requested that the customs exemptions granted to products listed under serial nos. 166, 167 and 217 via customs notification no. 50/2017 by the Government of India should be continued and should not be removed.

Several more products listed under serial nos. 166 via customs notification no. 50/2017 mentioned as below should be continued and should not be removed.

S. No.	Drug/Molecule	Serial No.	Concessional Rate of Duty as per the notification
1.	Tobramycin	166	5%
2.	Tretinoin	166	5%
3.	Ursodeoxycholic Acid	166	5%
4.	Vecuronium Bromide	166	5%
5.	Zidovudine	166	5%
6.	Efavirenz	166	5%
7.	Emtricitabine	166	5%
8.	Entacevir	166	5%

Retain the exemption for Entry 481 of Notification no. 50/2017-Customs dated 30/06/2017 which reads as "Disposable sterilised dialyser and micro barrier of artificial kidney"

Background

In India, as per the data published on the National Health Portal by the Government of India, "*Every year 2.2 lakh new patients suffering from ERSD get added to the overall count of patients taking the demand for dialysis treatment to almost 3.4 crore dialysis every year*"

A 2018 estimate put the number of patients on chronic dialysis in India at about 175,000, giving a prevalence of 129 per million population (1). The number of deaths attributable to CKD in India rose from 0.59 million in 1990 to 1.18 million in 2016 (2). HD (Haemodialysis) is the most common modality as renal replacement therapy and estimated to have about 1,20,000 patients on HD. Even today, over 90% of patients requiring RRT in India die because of inability to afford care, and even in those who do start renal replacement therapy, 60% stop for financial reasons (3). According to report from a state-wide database, about 49% of patients stopped dialysis and 13% died within 1 year. The reasons for poor outcomes are unclear but are postulated to be a mix of financial burden, multiple comorbidities, poor access, and poor dialysis quality (4)

Impact: Imposition of Customs duty on Dialyzers will result in increase in the overall cost of dialysis treatment and be an additional burden on the patient. Any Customs Duty imposed on import of Dialyzers would only increase the cost of dialysis process in the hands of the patients. It is important to note that as per data publicly available, lakhs of patients in India drop out of dialysis treatments due to lack of funds and the treatment being too expensive. In such a grim scenario in the country, any increase in cost of dialysis will take the whole dialysis infrastructure of the country back by many years**.**

It is an unfortunate fact that the current infrastructure meets less than half of the demand for dialysis centres. This results in a monthly expenditure of approximately INR 2000 per session, and around INR 3-4 lakhs per year (data source – nhp.gov.in). In such a situation, the Government of India has also launched the Pradhan Mantri National Dialysis Program (PMNDP) to give special focus to this sector and set up Government dialysis centres to make this treatment available for all and sundry.

For business and economic reasons, any non-creditable taxes levied on import of Dialyzers required for dialysis treatment will have to be passed on by the importers to their customers (dialysis centres, hospitals, etc.) and so forth making the treatment even more expensive for patients in India. This will be against the overall objective of the Government behind the Pradhan Mantri National Dialysis Program (PMNDP).

While the Government has been taking a lot of encouraging steps in this area, the domestic manufacturing of dialysers is not sufficient to cater to the increasing demand. There is still a significant dependency on imported Dialyzers with innovative technology for effectively treating patients in India. Imposition of additional non creditable taxes, such as Basic Customs Duty (and consequential social welfare surcharge), on Dialyzers required for dialysis treatment would further increase the cost of treatment making it unaffordable for a large segment of the Indian population.

Hence, exemption under Entry 481 of Notification no. 50/2017-Customs dated 30.06.2017 should be retained to ensure that the patients do not have to incur any additional cost in treatment due to non-creditable taxes being imposed on import of dialyzers into India**.**

Reference:

1. Jha V, Ur-Rashid H, Agarwal SK, Akhtar SF, Kafle RK, Sheriff R; ISN South Asia Regional Board: The state of nephrology in South Asia. Kidney Int 95: 31–37, 2019 10.1016/j.kint.2018.09.001

2. Xie Y, Bowe B, Mokdad AH, Xian H, Yan Y, Li T, Maddukuri G, Tsai CY, Floyd T, Al-Aly Z: Analysis of the Global Burden of Disease study highlights the global, regional, and national trends of chronic kidney disease epidemiology from 1990 to 2016. Kidney Int 94: 567–581, 2018 10.1016/j.kint.2018.04.011

3. Varughese S and Abraham G, Chronic Kidney Disease in India, A Clarion Call for Change. Clin J Am Soc Nephrol 13: 802–804, 201

4. Joyita Bharati and Vivekanand Jha titled *Global Dialysis Perspective: India*; *KIDNEY360 1: 1143–1147, 2020. doi: https://doi.org/10.34067/KID.0003982020*

Retain the complete exemption from Basic Customs Duty provided on import of 'Artificial Kidney' as per Entry 216 of Notification No. 50/2017-Customs dated 30.06.2017

Background: A 2018 estimate put the number of patients on chronic dialysis in India at about 175,000, giving a prevalence of 129 per million population (1). The number of deaths attributable to CKD in India rose from 0.59 million in 1990 to 1.18 million in 2016 (2). HD (Haemodialysis) is the most common modality as renal replacement therapy and estimated to have about 1,20,000 patients on HD. Even today, over 90% of patients requiring RRT in India die because of inability to afford care, and even in those who do start renal replacement therapy, 60% stop for financial reasons (3). According to report from a state-wide database, about 49% of patients stopped dialysis and 13% died within 1 year. The reasons for poor outcomes are unclear but are postulated to be a mix of financial burden, multiple comorbidities, poor access, and poor dialysis quality (4)

Impact: Imposition of Customs duty on artificial kidneys will result in increase in the overall cost of dialysis treatment and be an additional burden on the patient. Any Customs Duty imposed on import of dialysis equipment would only increase the cost of dialysis treatment in the hands of the patients. It is important to note that as per data publicly available, lakhs of patients in India drop out of dialysis treatments due to lack of funds and the treatment being too expensive. In such a grim scenario in the country, any increase in cost of dialysis will take the whole dialysis infrastructure of the country back by many years.

For business and economic reasons, any non-creditable taxes levied on import of equipment required for dialysis treatment will have to be passed on by the importers to their customers (dialysis centres, hospitals, etc.) and so forth making the treatment even more expensive for patients in India. The Government of India has launched the Pradhan Mantri National Dialysis Program (PMNDP) to make dialysis more affordable and reachable to all. Increase in cost of dialysis by levying Custom Duty will be against the overall objective of the Government behind the PMNDP. Hence, it is of utmost national importance to continue the exemption on 'Artificial Kidney' under the Customs Tariff Act.

Request for Consideration: While the Government has been taking a lot of encouraging steps in this area, the domestic manufacturing of such artificial kidneys, i.e., dialysis machines and dialysers is not enough to cater to the increasing demand. There is still a significant dependency on imported dialysis equipment for effectively treating patients in India. Imposition of additional non creditable taxes, such as Basic Customs Duty (and consequential social welfare surcharge), on equipment required for dialysis treatment would further increase the cost of treatment making it unaffordable for a large segment of the Indian population. It is, therefore, imperative for the Government to continue with exemption on import of "Artificial Kidney" to keep dialysis treatment affordable.

Issue suitable clarification stating that dialysis machines qualify as 'artificial kidney' under S.No..216 of Notification no. 50/2017-Customs dated 30.06.2017

Background: Entry no. 216 of Notification No. 50/2017-Customs dated 30.06.2017 is read as: "Any Chapter- Artificial Kidney". The term Artificial Kidney has not been defined under the Customs provisions. As a result of this, varying interpretations are being taken by field

officers of the Customs department for determining what would qualify as 'artificial kidney' for the purpose of the exemption. In some cases, due to this interpretational issue, exemption available is also questioned by the officers.

Artificial kidneys are dialysis machines and dialysers which are used for patient suffering from end stage kidney disease (ERSD). For patients suffering from ERSD, dialysis is a key treatment prescribed by doctors.

Further, under the National Health Mission, the Ministry of Health and Family Welfare has issued the National Dialysis Program as an initiative to reduce the financial burden of dialysis on patients. The said program has been issued after consultation with multiple health experts as quoted in the tender document. Page 1 of the tender document is reproduced as under:

> *'Hemodialysis (HD, commonly known as blood dialysis): In HD, the blood is filtered through a machine that acts like an* ***artificial kidney*** *and is returned back into the body. HD needs to be performed in a designated dialysis centre. It is usually needed about 3 times per week, with each episode taking about 3-4 hours.'*

As per the medical fraternity, dialysis machines and dialyzers are *de facto* artificial kidney as they perform the activity which is performed by a human kidney. Also, in medical circles, there is no other product which is an artificial kidney other than dialysis equipment.

Hence, it is requested that in addition to the continuance of exemption, a clarification be issued that 'artificial kidney' covers dialysis machines as well.

Reference:

5. Jha V, Ur-Rashid H, Agarwal SK, Akhtar SF, Kafle RK, Sheriff R; ISN South Asia Regional Board: The state of nephrology in South Asia. Kidney Int 95: 31–37, 2019 10.1016/j.kint.2018.09.001
6. Xie Y, Bowe B, Mokdad AH, Xian H, Yan Y, Li T, Maddukuri G, Tsai CY, Floyd T, Al-Aly Z: Analysis of the Global Burden of Disease study highlights the global, regional, and national trends of chronic kidney disease epidemiology from 1990 to 2016. Kidney Int 94: 567–581, 2018 10.1016/j.kint.2018.04.011
7. Varughese S and Abraham G, Chronic Kidney Disease in India, A Clarion Call for Change. Clin J Am Soc Nephrol 13: 802–804, 201
8. Joyita Bharati and Vivekanand Jha titled *Global Dialysis Perspective: India*; *KIDNEY360 1: 1143–1147, 2020. doi: https://doi.org/10.34067/KID.0003982020*

Serial No. 167 of Notification No. 50/2017 – Customs dated 30th June, 2017

Sr. No. 167 (A) of the aforementioned notification provides full exemption from Basic Customs Duty (BCD) to diagnostic kits specified in list 4 which includes "Diagnostic Kits for detection of HIV antibodies" at Sr.No. 28 in List 4. It is pertinent to note that the entry "Diagnostic kits for detection of HIV antibodies" which enjoys exemption as on date under List 4 have been inserted in the customs Tariff in the year 1989 vide amendment

Notification: 209/89-Cus. dated 17-Jul-1989 to amend Notification No. 208/81 - Customs (G.E.100).

The above entry covers within its ambit only those diagnostic kits which help in diagnosis of HIV using Serologic Diagnosis i.e. Antibody Testing. However, there is no specific exemption available which can be extended towards Diagnostic kits using Nucleic Acid Amplification Testing (NAAT - Molecular Testing) which also help in diagnosis of HIV. Therefore, we would request your consideration towards providing a suitable upfront exemption from Customs duty for the finished RT-PCR diagnostic testing kits imported for diagnosis of HIV. It is emphasised that both methods of diagnostic testing have their own particular nuances however, the RT-PCR diagnostic tests have a clear technological advantage over ELSIA Kits in producing accurate and reliable test results. Since any type of diagnostic test kits will play a major role in the fight against elimination of HIV and prevention and diagnosis of HIV in India though accurate testing & diagnosis, the exemption shall be available to all types of kits irrespective of the type of methodology adopted for detection. Thus our suggestion is that the above entry should be suitably amended to remove the word “antibodies” and to be read as **“Diagnostic kits for detection of HIV”** which will cover within its ambit all types of diagnostic kits for diagnosis of HIV.

It is apparent that this entry is enjoying exemption for the past 32 years and have not undergone any change till date and are still appearing in the customs tariff under the exemption notification category. It is undeniable that in the last three plus decades the advancement in technology and research in the field of medical science has been phenomenal. We would like to draw attention to the fact that this exemption has not undergone a change in the same pace in which the diagnosis testing methodologies have advanced in these three plus decades. Therefore, there arises a need to re-look at this exemption notification which provides exemption to ELISA kits and Antigen/Antibody testing (Serologic Diagnosis) which are primitive testing methods in comparison with the Nucleic Acid Amplification (NAAT Testing) molecular tests which are far more reliable and provide elaborate results for diagnosis. It is evident and over the years it has also been demonstrated Nucleic Acid Amplification Testing (NAAT) is more sensitive than standard serologic testing in detection. Further, in comparison to the serologic diagnosis, RT-PCR tests are more convenient, reliable and the most preferred option in todays time which provides more accuracy in terms of diagnosis of HIV in affected person. Since both type of testing are used in the diagnosis and detection of HIV, we are of the view that all type of detection kits for diagnosis of HIV should enjoy similar exemption.

Under the notification 167 (A) list 4, Serial Number 32 there is duty exemption for Enzyme Linked Immunoabsorbent Assay Kits ELISA KITS.

Our suggestion would be to extend this notification to all kind of RTPCR Test Kits.

Under the notification 167 (B) there is duty exemption against IGCR(import of goods under concessional rate of duty) for Bulk drugs used in manufacture of life saving drugs or medicines at (A).

Our suggestion would be to extend this notification for reagents and raw materials required for manufacturing of all kind of RTPC Test Kits.

Paraxylene (HS code: 29024300), vide Notification no. 50/2017-Customs dated 30th June 2017 (serial no. 196)

Paraxylene (PX) is the basic feedstock for the entire polyester industry. India has a thriving polyester industry, which is going to play an even more important role in the Indian textiles sector going forward as there is very limited scope for increasing production of cotton.

Paraxylene is used to produce Purified Terephthalic Acid (PTA), which is a key fibre intermediate for polyester. Being a key pillar of the polyester value chain, self sufficiency in PTA is critical for a robust domestic textile industry. This is also in line with the Hon'ble PM's vision of "Atmanirbharta".

India already has a significant domestic capacity of PTA of over 6 million MT, which is adequate to meet current demand, and is in the process of adding another 2.5 million MT in the next few years. However, when compared to China's PTA capacity of around 54 million MT, India has a long way to go. Withdrawal of the duty exemption for PX will inhibit the competitiveness of domestically manufactured PTA and discourage PTA capacity addition. Consequently, India will be increasingly dependent on imports for sourcing of PTA and value addition and employment creation in this part of the value chain will happen elsewhere rather than in India.

To ensure minimum reinvest economics for PTA, it is necessary that there is at least a 5% duty spread between PX and PTA. The existing duty differential between Paraxylene and PTA stands at 6.5% in USA, 5.3% in Japan and 5% in China. This has been done to ensure the development of this part of the value chain, which is necessary for the development of the overall textile industry.

Today textile industry is a second largest employment generator and also lifeline for Indian Industry. To achieve Prime Minister's vision for growth of Indian textile industry from US$ 140 billion to US$ 350 billion, the country would need large investment of above US $ 15 billion in polyester upstream and almost US $ 5-7 billion in downstream.

These investments will make India self-sufficient for its domestic industry requirement and also target international markets in value added products to the tune of US $ 100 – 125 billion. India needs to expand aggressively on Weaving and processing; Garmenting; Medical Textile; Geo Textile; Home Textile; Technical Textile; Industrial Textile as well as Speciality products for Defence.

For the growth of the polyester sector and realising the vision of Atmanirbhar bharat, it is imperative that all segments of the value chain attract investments and grow. Continuation of the duty exemption on Paraxylene will be a right step in that direction.

SECTORAL ISSUES

AGRICULTURE

1. Reduce rate of tax for the companies providing Agricultural Linked Services

Issue

The reduced rate of tax of 15% is not available to the companies engaged in providing agricultural services. Companies in business of agricultural services have largely low margins.

Recommendation

- To reduce the burden of cost on agricultural produce, it is recommended that companies whose more than 50% turnover comes from providing services directly related to agriculture may be taxed at a concessional rate of 15%. It will help the companies to grow and provide better professional services in the agricultural sector.
- TDS rates on services like storage, collateral management and warehouse management services may also be reduced from the current rate of 10% to 2%. This will help in easing working capital issue due to cash blocked in tax refunds.

Justification

The reduction of tax rate as suggested above will enable the companies to reduce the blockage of funds and invest them in enhancement of their scientific storage capacity and infrastructure thereby ensuring sustainability and progress in the sector.

2. Restore weighted deduction of 200% in respect of Research and Development expenditure (R&D)

Issue

The Finance Act, 2016, with a view to phase out weighted deduction under section 35(2AB) of the Income Tax Act, 1961 (‘the Act’) restricted the allowability of expenditure incurred on research and development in agriculture sector to 150% from 200% with effect from April 1, 2017 to March 31, 2020 and to 100% from previous year 2020-21 onwards.

Recommendation

Considering relevance of research and development investment for Indian economy and agriculture we request for restoring 200% income tax deduction for R&D expenditure.

Justification

India is globally recognized as an attractive jurisdiction for outsourcing owing to its affordable and skilled manpower. Outsourced R&D work is becoming a key area of growth for the Indian agriculture sector. However, there are no specific tax benefits available to units engaged in the business of R&D. Such tax benefits are the need of the hour to foster the growth of R&D segment and help achieve the Hon’ble Prime Minister’s vision to turn India into a research powerhouse.

3. Recommendations regarding Pradhan Mantri Matsya Sampada Yojana (PMMSY)

Pradhan Mantri Matsya Sampada Yojana is a scheme to bring about Blue Revolution through sustainable and responsible development of fisheries sector in India. The PMMSY is designed to address critical gaps in fish production and productivity, quality, technology, post-harvest infrastructure and management, modernisation and strengthening of value chain, traceability, establishing a robust fisheries management framework and fishers welfare. Few recommendations regarding PMMSY scheme are mentioned below:

a] Increase allocation of Rs. 1 Lakh per boat to Rs. 3 Lakhs per boat

Existing Position

Section 11.1-point (ii) PMMSY says "The safety kit may consist of GPS, life jacket, lifebuoy and other lifesaving appliances, a radar reflector, first-aid box, a set of flares, backup battery, search & rescue beacons etc., (other than Communication and/or Tracking Device). Within the ceiling of Rs. 1 lakh unit cost, the States/UTs, after due-diligence and based on essentiality are free to seek central financial assistance for all or some or any one individual essential item of safety kit.

Issue

The allocation of Rs. 1 Lakh per boat is not sufficient to cover all safety devices mentioned under PMMSY. Strengthening of safety and security of fishermen needs attention.

Recommendation

Allocation of 1 Lakh per boat to be increased to 3 Lakhs per boat.

Justification

The allocation of Rs. 1 Lakh per boat is not adequate to cover all safety devices mentioned under PMMSY scheme Section 11, which mentions that safety kit may consist of GPS, life jacket, lifebuoy and other lifesaving appliances, a radar reflector, first-aid box, a set of flares, backup battery, search & rescue beacons.

A single GPS device costs close to Rs. 75000. Secondly in current allocation, there is no mention of cost of marine radios and recurring cost of using marine radio licenses for marine fisherfolks and cost of installing and using them month on month.

b] Increase allocation of Rs. 11000 to Rs. 2 Lakh for Potential Fishing Zone (PFZ) device

Existing Position

Section 11.3 mentions allocation of Rs. 11000 for PFZ.

Issue

Marine network is negligible in the ocean, so giving the PFZ device without a strong communication system in place defeats the purpose.

Recommendation

Rs. 11000 allocation to be increased to Rs. 2 Lakh for PFZ.

Justification The unit cost of the PFZ device also includes installation and annual maintenance of PFZ devices for a period of 5 years.

It is important to support Fishermen for PFZ devices and network including the cost of installation and maintenance etc. A device that will show PFZ to marine fisherfolks needs good infrastructure to receive the information from shore across a solid network.

The cost of providing the communication support is approximately Rs. 1 Lakh which will cover other costs like base stations, nano stations, orbiters, modems, weatherproof walkie talkies and cell phones etc.

c] Increase proposed budget of Rs. 3000 per year to Rs. 3500 per month of the fishing ban

Existing Position

One activity namely "Livelihood and nutritional support for socio economically backward, active traditional fishers‟ families for conservation of fisheries resources during fish ban/lean period" under PMMSY is continued as per the norms, guidelines and funding pattern of the Saving-cum-Relief Component of the Centrally Sponsored Scheme (CSS) - Blue Revolution Scheme: Integrated Development and Management of Fisheries. Accordingly, the governmental assistance of Rs. 3000 per annum per enrolled beneficiary under this activity under PMMSY are shared as detailed below:

(a) The North Eastern & the Himalayan States: 80% Central share and 20% State share.

(b) Other States: 50% Central share and 50% State share.

(c) Union Territories (with legislature and without legislature): 100% Central share.

Issue

Livelihood and nutritional support provided for socio-economically backward active traditional fishers families for conservation of fisheries resources during fishing ban/lean period is not sufficient.

Recommendation

The proposed budget of Rs. 3000 per year to be increased to Rs. 3500 per month of the fishing ban.

Justification

The duration of the ban is different in different states. In some states, it is for 1 month and in others it ranges from 2 or 3 months. The need for the ban is to stop fishermen fish during monsoon fish breeding season. However, with current allocation of amount, fishermen are forced to go for fishing to fed themselves and their family.

The allocation during ban period should be such that they can happily forget marine fishing for 2 months. This amount can be further made specific into segmenting it for small-mid and large-scale fisheries.

d] Add weather insurance to the PMMYS Scheme

Issue

Fishermen are increasingly losing business due to climate change induced weather abnormalities. This is increasingly becoming an opportunity area of insurance but there are no providers for a pocket friendly insurance product for fisherfolks.

Recommendation

Weather insurance should be added to the PMMSY scheme

Justification

The fishing industry is the most impacted due to unpleasant weather. Fishermen not only loose their catch but also their lives. Given the kind of risk they take at every trip, it's very important to provide insurance coverage. Insurance for their catch or non-availability of catch is important. Once the Government makes such a move, the private sector will also follow with more such offers.

INFORMATION TECHNOLOGY (IT) AND TELECOMMUNICATIONS

Direct Tax

1. Provide carry forward and set off of losses for telecom sector till 16 years instead of current provision of 8 years

Existing Law

As per section 72 of the Act, the taxpayer is allowed to carry forward non-speculative business loss to next eight assessment years from the assessment year in which the loss was incurred.

Issue

Telecom industry is going through a rough phase and lapse of losses post eight years will be detrimental to Telecom Industry as the income during recovery phase will be subject to tax outflows.

Recommendation

It is recommended that a special regime for Telecom Industry should be introduced in section 72 of the Act wherein the losses can be carried forward and set off till 16 years instead of 8 years.

Justification

Telcom Industry has been under tremendous business pressure and ongoing Covid epidemic since last two years has also had adverse impact on the business which has resulted into cumulative losses. These losses are unlikely to be set-off in next eight assessment years as provided under the current regime.

2. Provide clarity in definition of "Technical Services" and "Professional Services" under section 194J of the Act

Existing Law

The Finance Act, 2020 has reduced the TDS rate under section 194J to 2% (from existing 10%) in case of fees for technical services (FTS) payments. The amendment was made to end the dispute arising out of characterization dispute between section 194C and section 194J of the Act and issue of short deduction thereof.

Issue

While provision of 2% rate for FTS payments is a welcome change, the amendment will give rise to a new litigation in the form of distinction between professional services and technical service. Thus, such selective amendment for providing lower rate only for FTS payments is in direct conflict with the rationale in the Explanatory Memorandum to the Finance Bill, 2020 that it is intended to avoid litigation on short deduction issues.

Recommendation

- It is recommended that the TDS rate in case of "fees for professional services" under section 194J of the Act should also be reduced at par with rate provided under section 194C of the Act to achieve true parity and avoid further litigation on professional services v. technical services (FTS).
- TDS rate benefit of 2% should also be provided to telecom operators.

Justification

TDS @ 2% would be closer to the actual tax liability of Telecom Operators as margins earned by them are low and they sustain only on volumes.

3. Provide clarity on TDS on prepaid distributor margins/discounts from telecom operators

Existing Law

Section 194H of the Act provides for tax deduction at source on any income by way of commission or brokerage, by any person responsible for paying to a resident. TDS under this section is applicable only if the relationship between parties is of principal to agent.

Issue

Telecom companies transfer prepaid vouchers and talk time to the channel partners/distributors at discount. There has been continuous litigation on applicability of TDS on spread between maximum selling price and discounted price at which such products are transferred to the distributors. Telecom companies have long been contending that relationship between the company and distributors is of "Principal to Principal" and not "Principal to Agent" basis. Tax authorities have, however, been alleging that relationship between the Telecom company and distributors is of a Principal-Agent (and not a Principal-Principal) and thus, discount extended to distributors qualifies as 'commission' subject to tax withholding under section 194H of the Act.

Recommendation

It is recommended that the Government should issue a retrospective clarification that such discounts do not fall within the ambit of TDS provisions, or it may introduce special TDS rate of 1% which would be closer to the actual tax liability of distributors as margins earned by the distributors are low and they sustain only on volumes.

Justification

The relationship between the company and distributors is of "Principal to Principal" and not "Principal to Agent" basis. Thus, tax withholding under section 194H of the Act should not be attracted.

4. Rationalise definition of Industrial Undertaking

Existing Law

Currently, Section 72A of the Act allows carry forward of loss and accumulated depreciation in case of amalgamation/demerger of the following type of companies: -

- a company owning an industrial undertaking or a ship or a hotel with another company,
- a banking company,
- one or more public sector company or companies engaged in the business of operation of aircraft.

Issue

The benefit is not available to all the companies engaged in the business of providing services. Considering the facts that many multinational companies have entered in the Indian service market and it has become imperative for the small companies to consolidate their resources to survive.

Recommendation

The benefit applicable under the provisions of Section 72A of the Act should be extended to all companies irrespective of their line of operations.

Justification

The amendment will facilitate smooth operational reorganization across the economy including infrastructure sector if the benefit of this provision is provided to service providers such as Telecom Infrastructure Service Provider (TISP) and Direct-to-Home (DTH) operators etc.

Customs

5. Reduce customs duties on telecom equipment classified under chapter 8517 of the Customs Tariff

Existing Law

Currently, telecom equipment attracts basic customs duty (BCD) at the rate of 20%

Issue

Majority of the imported products used in the Telecommunication Network falls under the category of chapter 8517 and more specifically under the exception category of 85176290 which attracts Basic Customs Duty as high as 20%. In the event of critical goods being imported due to absence of these products in the domestic market, the higher duty is causing hardship for the telecom industry under the current economic situation.

As of today almost all Telecom equipments are subjected to BCD at 20% as can be seen below:

- BCD of 10% was introduced on various Network equipment from July, 2014
- From August, 2017 all the Network equipment's except Routers were saddled with BCD of 10%
- BCD was increased from 10% to 20% from October, 2018 on network equipments.
- Certain exemptions have been granted on telecom equipment, however, it contains an exclusion clause for latest technologies including 4G/LTE, MPLS, OTE, OTN etc. Thus, effectively, reducing the scope of the exemption on telecom equipment

Recommendation

It is recommended that exemption from the levy of BCD should be granted for all the technologies of the telecom equipment without any exclusions.

Justification

Telecom Industry is highly capital-intensive Industry and since telecom equipments are not manufactured in India, they have to be imported resulting in increased capex cost by 20%. The impact of increase in cost due to BCD is in the range of around Rs. 800 to 1,400 crores on each of the Telecom operators depending on capex rollout plans. This further aggravates the stress that the telecom companies are going through. Removal of BCD on Telecom equipment will not only help the Telecom companies in this difficult phase but will also expedite faster roll out of network and better quality of service.

PAPER AND PAPER BOARD

1. Increase Customs duty on import of Paper and Paperboards in line with agricultural products

Issue

The economic slowdown in developed economies and export dependent economies has led to severe excess capacity of Paper/Paperboard in paperboard manufacturing countries. Taking advantage of the low Customs Duty rate of 10%, these countries find India as an attractive outlet for diverting their excess inventory thus, hampering the domestic industry.

Recommendation

In order to provide a level playing field to the domestic industry it is recommended that:-

a) the Customs duty for import of Paper and Paperboards be increased to 25% and brought in line with agricultural products (which ranges up to 40%).

b) this category be kept in the Negative List (i.e., no preferential treatment) in bi-lateral and multi-lateral trade treaties and agreements.

Justification

The Indian Paper/Paperboard industry has made significant capital investments to ramp-up capacities for meeting domestic requirements. The Industry has strong backward linkages with the farming community from whom wood (raw material for manufacture) is sourced. A large part of this wood is grown in backward marginal/sub-marginal lands, which are potentially unfit for other use. The paper industry, being mainly located in backward areas, has transformed the socio-economic conditions of the population residing there.

Thus, whilst domestic industry is operating under extremely challenging conditions, substantial quantities of paper and paperboard is imported into the country at significantly lower costs. This is bound to discourage investments towards capacity enhancement by the domestic industry, notwithstanding the fact that such investments will be necessary to cater to the expected growth in demand for paper and paperboards. The inevitable consequence of drop in investments will be a multiplier adverse impact on the Indian farmer community with whom the industry has strong linkages and a significant outflow of foreign exchange towards increased imports of paper and paperboards.

2. Provide Incentives for Investments in Environment Friendly “Clean” Technologies by Paper Industry

The broad policy framework on environment and climate change in India is laid down by the National Environment Policy (NEP) 2006 which aims to chart the way forward to meet the Government’s bold announcements in the energy domain like target of reduction of emissions intensity by 33%-35% by 2030 over 2005, share of non-fossil fuel-based capacity in the electricity mix aimed at above 40% by 2030 etc.

India has a definite plan of action for clean energy, energy efficiency in various sectors of industries, a major thrust to non-fossil based electricity generation and a building sector based on energy conservation. In this context, NITI Aayog, Government of India has published the ‘Draft National Energy Policy’ to enable meeting the goals of renewable energy capacity, emission intensity and non-fossil fuel share in the electricity mix of India by the year 2030.

India meets its energy requirements predominantly through fossil-based sources (coal). A significant portion of such energy is used to operate Industries such as Aluminium, Cement, Chlor-Alkali, Fertilizer, Iron & Steel, Pulp & Paper, Textile, Thermal Power Plants, Oil Refineries, Electricity Distribution Companies and Railways. Incidentally, Government has already identified these Industries as focus area to reduce energy consumption, under Energy Conservation Act, 2001.

Most of these Industries have installed Captive Power plants operating Boilers on Fossil fuel such as Coal, Natural gas etc. The renewable energy portion is limited to few cases even though opportunities exist to increase the footprint**.** It is important that Boilers operating on renewable energy sources such as bio-mass are also encouraged with appropriate incentives.

CIGARETTES

1. Reduce taxes on cigarettes

Issue

The increase in National Calamity and Contingent Duty (NCCD) on cigarettes in the Union Budget of February 2020, resulted in a 13% increase in tax incidence. Subsequent to such increase, the tax revenues have de-grown by 4% during the period February 2020 to June 2021 as compared to the period April 2019 to January 2020. In contrast, the relative stability in cigarette taxes, between July 2017 and January 2020 contributed to the growth in revenue collections. This is corroborated by the fact that during the period April 2018 to January 2020, there was a revenue growth of 10.2%, as compared to the period of July 2017 to March 2018. It is evident that revenue collection from cigarettes will continue to suffer if tax rates remain high.

Recommendation

It is recommended to consider a reduction of tax on cigarettes which would help the legal industry to recoup volumes from the illicit trade and provide higher revenues to the Government. Any increase in taxes will provide further impetus to the illicit trade and adversely impact revenue collection.

Justification

The unprecedented disruption in the market due to the lockdown consequent to the Covid 19 pandemic, followed up by geography specific restrictions imposed by state / local authorities in the wake of second wave during Q1 FY 2021-22, has had a disastrous impact on the legal cigarette industry. Taking advantage of the supply chain disruptions, unscrupulous elements have been emboldened to drastically increase the illicit trade to unprecedented levels.

As per the reply given by the Union Minister of State for Commerce & Industry in the Lok Sabha on 17 March 2021, enforcement agencies in India have seized illicit cigarettes/ exposed tax evasion worth over Rs 1700 crore in 2020-21 (till Feb 2021) which is a quantum jump of more than 9 times compared to last year. It is estimated that revenue loss on account of duty-evaded cigarettes cost the exchequer of almost Rs. 15,000 crores in revenue every year.

2. NCCD on Tobacco and Tobacco Products be abolished

Issue

Tobacco and tobacco products are the only goods on which both National Calamity and Contingent Duty (NCCD) and GST are levied. Not only is this discriminatory but is also against one of the primary objectives of GST, i.e., elimination of cascading of taxes.

Recommendation

Continuation of NCCD is a retrograde step and, accordingly, the Government is requested to consider its abolition.

Justification

In line with abolition of cesses on other goods and services the NCCD levy on tobacco and tobacco products also merits abolition.

FURNITURE

1. Provide Zero Customs Duty on Select Raw Material

Issue

Limited Availability of certified raw material is a challenge for furniture industry. It may be noted that below mentioned goods with Forest Stewardship Council (FSC) and California Air Resources Board (CARB) certifications are not easily available in India. This is currently produced in very low volumes by Indian manufactures, as domestic industry or domestic consumption does not require such certificates. Hence, by eliminating duties on certified material, domestic industry will not be affected and may continue to be protected.

Formaldehyde emulsion in CARB certified MDF/Plyboard and Particle board is very low in comparison to non-CARB certified MDF/Plyboard and Particle board. The global market only allows import of furniture manufactured through CARB certified MDF/ Plyboard and Particle board. In India, we have a number of factories producing non-CARB certified MDF/Plyboard and Particle board, this is cheaper and easily consumed in local market as India do not have any CARB policy. In fact, we understand that DPIIT is already considering reduction in BCD from existing 5% to 0% on the following item HS code 4401 (Fuel Wood),4402 (Wood Charcoal) and 4403 (Wood in Rough).

Recommendation

It is requested that the Government may consider zero custom duty on the following raw materials provided that they are FSC/PEFC/CARB certified.

S No.	Material	HS CODE
1	Wood in Rough	4403
2	Sawn wood	4407
3	Veneer	4408

4	Particle Board	44101110
5	HDF boards	44119211
6	MDF boards	44111400

2. Introduce Phased Manufacturing Programme

To encourage domestic furniture manufacturing, phased manufacturing programme, wherein BCD can be increased @2.5% per annum for next five years, shall be introduced. Proposed phase wise increase of BCD is given in the below chart. The roadmap for Phased Manufacturing Programme for Furniture Industry is given below: -

Sr No.	Item Description	HS Code	Current BCD%	Proposed phasing of BCD%				
				Y1	Y2	Y3	Y4	Y5
1	Office Furniture of Metal Other Than Steel	94032090	25	27.5	30	32.5	35	37.5
2	Furniture Components & Parts	94039000	25	27.5	30	32.5	35	37.5
3	Furniture of Other Material not of Plastic, Bamboo, Wood or Metal	94038900	25	27.5	30	32.5	35	37.5
4	Office Wooden Furniture	94033090	25	27.5	30	32.5	35	37.5
5	Wooden Furniture of Kitchen	94034000	25	27.5	30	32.5	35	37.5
6	Other Wooden Furniture	94036000	25	27.5	30	32.5	35	37.5
7	Wooden Sofa Sets	94035090	25	27.5	30	32.5	35	37.5
8	Beds	94035010	25	27.5	30	32.5	35	37.5
9	Upholstered Furniture	94016100	25	27.5	30	32.5	35	37.5
10	Ball bearing/runner telescopic drawer slides	83024200	15	17.5	20	22.5	25	27.5

11	Auto closing hings for cabinet	83021090	15	17.5	20	22.5	25	27.5
12	Aluminium profiles for furniture & sliding system	76042990	7.5	10	12.5	15	17.5	20
13	Aluminium profiles for furniture & sliding system	76041039	7.5	10	12.5	15	17.5	20
14	Aluminium profiles for furniture & sliding system	76109030	10	12.5	15	17.5	20	22.5

3. Allow the verification of compliances as post clearance in case of Participating Government Agencies (PGA) related clearances for AEO importer

Issue

While the intent of the customs authorities has been to reduce interaction with the trade and encourage a risk-based approach instead of Rule based approach to governance. The recent changes in policies and lack of enforcement of key enablers to Ease of Doing business like the AEO certification is still lacking. The customs rules have been changed to make Self-Assessment as primary mode of customs clearance. There is also AEO certifications being granted to large importers or importers who have demonstrated a will to comply to regulations and effective internal controls. This, however, has not seen major improvement in the customs intervention reduction in clearance. Risk Management system decides if a container will be opened for examination or if the customs officer will verify valuation and classification manually. This criterion has no impact on whether the importer is AEO accredited or not.

Recommendation

It is recommended to allow the verification of compliances as post clearance in case of PGA related clearances for AEO importer. This will reduce dwell time and provide a single point of verification for all PGA's and customs authorities.

4. Exempt Large importers who are AEO certified from the requirements of Phytosanitary certificates and post clearance testing

Issue

Currently the Plant quarantine regulations do not differentiate between furniture articles that have undergone processing before they have reached the current form. The criteria for verification and release from the PQ authorities is the Plant origin (wooden) for permission to be cleared by Plant Quarantine (PQ) and customs authorities. For example if Bamboo

fiber is used to make vessels / lids or tables where essentially the article does not retain the natural characteristics of Bamboo and have transformed into articles that cannot be infected by pests by virtue of the treatment (heat) used in the manufacturing of the resultant products. The law however, still requires that the importer gets a Phytosanitary certificate from the exporting country basis which the shipment will be released by the PQ authorities in India.

Another example is that furniture articles which are coated with paint or lacquer during manufacturer to avoid any form of infestation post manufacturing and during transport or storage till it reaches the end consumer. The law does not exempt such articles from the procedure of obtaining Phyto Sanitary certificates/PQ release.

Recommendation

It is recommended that large importers who are AEO certified should be exempted from the requirements of Phytosanitary certificates and post clearance testing as required may be done based on risk assessment of the officer/PQ authorities to verify presence of any insects /pests in the cargo. This will reduce the cost of documentation and will improve procedural simplification for reputed companies without increasing risk for the Indian authorities.

5. Exempt BIS certification for import of LED light Furniture fitting products

Issue

Currently, BIS certification is mandatory for import of LED Light products, designed to be fitted with Furniture's and for use in Interior Home decoration. This creates tremendous hardship as the volume of import of such fittings is very low but the process of getting them certified is very time consuming and complicated. These are high quality fittings that have to be imported in many cases under Chapter 85 of the Customs Tariff.

Recommendation

It is suggested to create separate sub code under chapter 85 for Furniture Fitting related LED lights to exempt them from BIS certification.

6. Reduce the custom duty on furniture child parts to 15%

Issue

Small components and parts required for manufacturing of furniture products are currently covered in HS code 94039000 ('Other Furniture Parts'). The customs duty rate on the same is 25% which is the same as for finished products covered in 9403. Rate of Custom Duty on child parts and components (Furniture fittings which make Furniture functional and help construction of Furniture), should be lower than the duty imposed on finished goods to ensure viability for the Indian manufacturer.

Recommendation

It is suggested to lower the custom duty on furniture child parts to 15% to bring parity with the customs duty rate on furniture fittings under code 83024200.

TOURISM

1. Allow deduction of Rs. 1.5 lakh on travel spending to boost the tourism sector

Issue

The tourism sector has been worst hit due to the unprecedented COVID-19 pandemic.

Recommendation

It is recommended that to allow a tax exemption for AY 2022-23 and 2023-24 to all employees with a maximum limit of Rs. 50,000 per person provided the employee spends a sum equal to three times the allowable exemption amount on hotel accommodation, airfare or any other travel related booking including tour packages which carry GST rate of at least 5% from a GST registered hotel, airline or a travel agent.

Alternatively, allow a deduction of Rs. 1.5 lakh under Chapter VIA of Income Tax Act towards the expenses on hotel accommodation, airfare or any other travel related booking including tour packages which carry GST rate of at least 5% from a GST registered hotel, airlines, or a travel agent.

Justification

In October 2020, the Government of India extended an income tax exemption for cash payment equivalent to Leave Travel Concession (LTC) fare to private sector employees. As per the scheme, the payment of cash allowances in lieu of LTC fare, with a maximum limit of Rs. 36,000 per person were exempted from tax provided the employee spends a sum equal to three times of the value of the deemed LTC fare on purchase of goods/services which carry a Goods and Services Tax (GST) rate of at least 12% from GST registered vendors/service providers through digital mode.

The initiative not only promoted public spending, it also motivated people to buy goods and services from GST registered suppliers and thereby boosted GST revenue. In the given circumstances, travel sector needs a similar push on travel spending.

2. Withdraw TCS on sale of foreign tour packages and foreign travel spending under liberalised remittance scheme (LRS) of RBI

Issue

The Finance Act 2020, which was announced just before the start of Covid-19 crisis in India, introduced TCS @5% on ‘sale of overseas tour packages by tour operators’ and on ‘foreign exchange remittances under LRS of RBI by authorised dealers (Banks)’.

In FY 2020-21 the sale of overseas tour packages has shrunk significantly, resulting in loss of significant business and jobs for numerous travel agents and tour operators in India. This also significantly affected the Government revenues in the form of GST payable on such business.

Recommendation

To save overseas tour packages business and related jobs in India it is recommended that the TCS provisions under section 206C (1G) sub-clause (a) and (b) of the Act on remittances under LRS and sale of overseas tour packages respectively, be withdrawn.

Justification

TCS @5% on sale of foreign tour packages by Indian Tour operators and on LRS remittances by AD/Banks lead to increase in the cost of travel. This also led to customers choosing foreign travel agents, tour operators or even prefer direct payments to foreign hotels, etc to save against TCS payments.

3. Introduce real-time API based functionality to verify such compliance against a particular PAN for purposes of TDS/TCS under section 206AB and 206CCA of the Act

Issue

Section '206AB' and '206CCA' in the Income Tax Act introduced vide Finance Act 2021, mandates tax deduction or collection at a higher rate for non-filing of returns in the previous two financial years. Section 206AB of the Act is related to the higher rate of TDS and 206CCA is for TCS. This section is effective from 1st July,2021.

The higher rate is applied for certain notified taxpayers referred to as 'Specified Persons". The expression 'specified person' means a person who has not filed the returns of income for both of the two assessment years relevant to the two previous years immediately prior to the previous year in which tax is required to be deducted, for which the time limit of filing return of income has expired and the aggregate of tax deducted at source in his case is rupees fifty thousand or more in each of these two previous years. These provisions cast an additional responsibility on the payer to deduct higher rate of tax on payments to persons who have not filed their returns of income for one of the preceding two assessment years. This creates significant additional compliance burden on the taxpayer to check whether the deductee has filed its tax returns for the last two years.

Recommendation

Since the Government has the data with respect to PAN details of the taxpayer who do not file their tax returns, therefore it is recommended that it should reconsider whether such additional compliance obligations are needed.

Nonetheless, till the time a real-time API based functionality is made available by CBDT to verify such compliance against a particular PAN the applicability of these provisions should be deferred.

Justification

CBDT has introduced a new PAN based functionality to verify the compliance against aforesaid sections. However, this functionality does not allow a real-time API based checking. In the absence of such real-time API based functionality it becomes infeasible for E-commerce operators to check compliance towards an online real-time transaction. Recovery additional TDS/TCS from customer once the transaction is already executed would lead to financial loss to the E-commerce operator.

NON-FERROUS METALS

Aluminium

1. Correct Inverted Duty Structure and Reduce Basic Custom Duty on critical raw materials for Aluminium Industry

The cost of production of aluminium metal in India has substantially increased due to rising cost of critical raw materials, inverted duty structure on import of raw materials, increase in various taxes/cess like Coal Cess, Electricity Duty and logistics costs etc. While other Aluminium producing countries support their domestic industry with cheaper raw material availability, power subsidies etc, India is struggling to retain competitiveness despite having natural advantage of 5th largest bauxite and 5th largest coal reserves in the world. The average production cost of Indian aluminium producers is amongst highest in the world, majorly due to high incidence of unrebated Central & State taxes and duties on inputs/raw materials accounting for more than 15% of Aluminium production costs.

China encourages import of raw materials at nil duty for Aluminium production to promote domestic value addition and generate employment & Forex with export of finished aluminium products. The high import duties on raw materials is a huge disadvantage for domestic aluminium producers which are heavily dependent on imported raw materials. It results in Indian finished goods costlier and uncompetitive in international markets, rendering negative protection against cheaper imports of finished products, and discourages domestic value addition within the country. To improve the cost structure of the Indian Aluminium industry and enhance competitiveness, it is requested to reduce the basic custom duty on the following critical raw materials as below:-

a. Caustic Soda Lye (HS Code 2815 12 00)

Issue

The import duty on Caustic Soda Lye (HS Code 2815 12 00) is 7.5% and duty on finished product alumina is 5%.

Caustic Soda Lye is a major raw material for Alumina production which is further used for production of Aluminium metal. Caustic Soda contributes to around 20% of Alumina production cost. India is a net importer of caustic soda and over 60% imports go to Aluminium industry. Aluminium industry is a bulk consumer of Caustic Soda, highly dependent on imports and not able to meet its demand through domestic sources due to several constraints related to quantity, infrastructure and logistics. (Majority of Caustic Soda production is in Western region (Gujarat, Maharashtra, Rajasthan) while major Alumina producers are in Eastern region (Odisha, Chhattisgarh, Andhra Pradesh, Uttar Pradesh), resulting in high logistics costs. The imports are already restricted due to BIS Standards (IS 252:2013) and Anti-Dumping duty is also in place on Caustic Soda imports from China and Korea.

Recommendation

It is recommended that the import duty of Caustic Soda Lye should be rationalized and reduced from 7.5% to 2.5%.

b. Calcined Petroleum Coke (HS Code 2713 12 10) and Raw Petroleum Coke (HS Code 2713 11 10)

Issue

Import duty on Calcined Petroleum Coke (HS Code 2713 12 10) is 7.5% and duty on finished product aluminium is 7.5%. Whereas, import duty on Raw Petroleum Coke (HS Code 2713 11 10) is 10% and duty on finished product CP Coke is 7.5%.

Aluminium industry uses Non-Fuel Grade CP Coke as a feedstock/process raw material for Aluminium production. It is not used for any fuel purpose in Aluminium industry. CP Coke is a crucial raw material and constitutes 6% to 8% of Aluminium production costs. The import duty on Pet Coke was increased from 2.5% to 10% on 14.12.2017 to restrict import of Pet Coke for usage as fuel purpose. It resulted in duty increase for Non Fuel Grade Pet Coke also.

Separate HS codes has been created for Raw Pet Coke and Calcined Pet Coke for use in Aluminium industry conforming with BIS standards (IS 17049:2018). The Hon'ble Supreme Court has also allowed Pet Coke imports for consumption in Aluminium industry with import quantity restriction of 0.5 million tons on CP Coke and 1.4 million tons on Raw Pet Coke, so duty reduction shall not result in any increased imports.

Recommendation

It is recommended that the inverted duty of raw & calcined pet coke be rationalized and reduced to 2.5%.

c. Aluminium Fluoride (HS Code 2826 12 00)

Issue

Import duty on Aluminium Fluoride (ALF3) is 7.5% and duty on finished product aluminium is 7.5%. AlF3 is a crucial raw material and constitutes 1.5% of aluminium production costs. India is a net importer of AlF3, and Aluminium industry importing 100% of its requirement.

Recommendation

It is recommended that the import duty of aluminium fluoride be rationalized and reduced from 7.5% to 2.5%.

d. Green Anodes/Pre-baked Carbon Anodes (HS Code 3801 90 00)

Issue

Import duty on Aluminium Fluoride is 7.5% and duty on finished product aluminium is 7.5%. The carbon anodes are used for electrolysis process of aluminium production, and 460 kg Anode is consumed for production of one ton aluminium metal. As these anodes are not produced domestically for commercial purpose, aluminium producers are sourcing these through imports to meet domestic requirement.

Recommendation

It is recommended that the import duty of green anodes/pre-baked carbon anodes be rationalized and reduced from 7.5% to 2.5%.

e. Calcined Alumina (HS Code 2818 20 10)

Issue

Alumina is a primary raw material for aluminium production constituting 35% of production costs. There is current deficit of 2.8 million tons per annum (mtpa) Alumina for meeting aluminium industry requirement, which can be met only through imports which are not economically viable due to high import duty of 5%. Against total Alumina requirement of 8.2 mtpa, the Alumina installed capacity is 7.28 mtpa, with captive production of 6.6 mtpa in FY-2021, and exports of 1.3 mtpa resulting in Alumina deficit. China supports its Aluminium industry with cheaper raw material availability by nil import duty on Alumina to encourage domestic value addition and production of finished aluminium products.

Recommendation

Being the primary raw material the import duty on alumina should be rationalized and reduced from 5% to nil to enhance raw material security for aluminium industry, this will encourage domestic value addition and exports of finished Aluminium products.

2. Rationalize Cess on Coal

Issue

The Coal Cess was introduced as Clean Energy Cess in 2010 with levy of Rs 50/ MT on coal. It has been repeatedly hiked over last few years- from Rs. 50/MT to Rs.100/ MT in 2014-15, increased to Rs.200/MT in 2015-16, and again increased by 100% to Rs. 400/ MT in the Union Budget 2016-17. The hike in coal cess has an impact of US$ 64/MT on Aluminium CoP, increased from US$8/MT. The Cess on coal replaced with GST Compensation Cess of equivalent value under GST regime to be levied only for the first 5 years from July 1st, 2017 to July 1st, 2022.

Year	Particulars	Cess Rate/ MT of coal	Impact ($/Ton) in Cop of Aluminium
2010	Introduced as Clean Energy Cess	**Rs 50/ MT**	**$ 8**
2014-15	Clean Energy Cess	Rs 100/ MT	$ 16
2015-16	Clean Energy Cess	Rs 200/ MT	$ 32
2016-17	Renamed as Clean Environment Cess	Rs 400/ MT	$ 64
2017-18	Replaced with GST Compensation Cess	**Rs 400/ MT**	**$ 64**

This steep hike in coal cess had adversely impacted the sustainability of aluminium industry being a highly Power intensive industries, where coal contributes to 40% of aluminium production cost. The cost of production of aluminium in India has substantially increased

primarily due to increased power cost over past few years with increasing coal prices, cess, RPO, ED, logistics cost etc.

In India the industrial power cost is very high despite having 5th largest coal reserves. Globally the major aluminium producing countries are extending support to bring down the power & production costs and rendering competitiveness to domestic aluminium industry.

A NITI Aayog report on "Need for Aluminium Policy in India" also highlighted the challenges of high-power costs for Indian Aluminium producers resulting in competitive disadvantage viz-a-viz global players:

Excerpts from NITI Aayog Report:

- *Amongst the largest producers of aluminum like Canada, Russia, Middle East, Norway and China,* ***India has the highest cost of production. This can be attributed to high power cost in India…***
- ***Coal cess alone amounts to almost 1/5th of the cost of mining coal****. Despite having a competitive advantage in coal,* ***India is one of the most expensive places to produce coal-based electricity****.*
- *High energy intensive sectors are being penalised by paying high carbon tax through various cesses...*

A separate energy policy for these industries should ensure that these industries receive power at globally competitive rates so that they can compete with global players. ***It is recommended that*** *RPO obligations,* ***coal cess and electricity duty charges may be rationalised to make these sectors competitive.***

Recommendation

It is recommended to eliminate the high cess on coal to support power intensive industries and retain competitiveness of domestic industry.

Copper

3. Reduce import duty for copper concentrate from 2.5% BCD at present to nil duty

Issue

At Present India is importing primary copper products & downstream products through various FTA routes at Nil Duty. To maintain the viability of industry and correct the inverted duty structure, government should reduce import duty on copper concentrate to Nil.

The copper concentrate is the primary raw material for refined copper production, the operational capacity of refined copper production is 1018 KT. The copper concentrate required for producing 1018 KT of refined copper is 3393 KT. At present, copper ore reserve in India is serving only 4% of copper concentrate requirement. Hence import of this raw material remains mandatory. The reduction in BCD for copper concentrate shall help domestic industry to compete with FTA imports.

Recommendation

It makes economic sense to exempt it from the customs duty. Given the non-availability of Copper Concentrate in India, there is no economic rationale to continue with Import Duty on Copper Concentrate and hence it is recommended that this is to be reduced (HS 2603) from 2.5% to Nil. This will enable the domestic industry to have a level playing field and compete with imports of Value-Added Copper products from FTA countries under NIL duty.

STEEL & OTHER FERROUS PRODUCTS

1. Reduce Basic Customs Duty on Ferro Nickel (HS Code 720460)

Issue

High Basic Customs Duty of 2.5% on Ferro Nickel

Recommendation

It is recommended to reduce the basic customs duty on Ferro Nickle to Nil from current rate of 2.5%.

Justification

a. Availability

- Ferro Nickel is the most important raw material for stainless steel making.
- The stainless-steel industry meets the bulk of its nickel requirements through Ferro Nickel and stainless-steel scrap route as pure Nickel is very expensive.
- Due to non-availability of Ferro Nickel in the country domestic stainless steel producers are forced to import it. This is because India is deficient in Nickel ore and therefore there is no production on Ferro Nickel within the country. There are no known producers of Ferro Nickel in India.

b. Procurement

- Most of India's Ferro Nickel is procured from Indonesia, Japan, South Korea and Greece.
- The Custom duty is not applicable on Ferro Nickel originating from Indonesia and Japan due to India- ASEAN FTA and India-Japan CEPA respectively but applicable on imports from countries including Europe and South America.

c. Changing global scenario

- After the pandemic, and the changing Chinese strategies of import and exports have led to higher booking by the Chinese of the Indonesian Nickel leaving low availability for other countries.
- Internationally too, the prices of raw materials including Ferro Nickel have been rising, in Q1 2021-22, prices have risen by 42% year on year. Also, with erratic supplies and serious availability issues, industry is facing a double whammy. This has led to Indian industry having to shift, Ferro Nickel procurement from outside Indonesia/Japan

exposing the Indian purchases to the applicable 2.5% BCD and not being able to take advantage of the operational FTAs.

- The cost impact of 2.5% import is a cost which stainless steel manufacturers in many other stainless steel producing countries like EU & USA don't have to bear as they have NIL duty on raw materials. This has the effect of placing the domestic stainless steel industry at a competitive disadvantage.

2. Continuance of Zero Customs Duty on Stainless Steel Scrap

Issue

Zero Customs Duty on Stainless Steel scrap is applicable only upto 31st March 2022.

Recommendation

It is recommended to continue zero Customs Duty on Stainless Steel scrap even after 31st March 2022.

Justification

The zero customs duty on Stainless steel scrap has helped the stainless steel industry in getting raw material for Stainless steel production at competitive rates at a time when the international stainless steel scrap prices have shot up by 25-40%. We are dependent on scrap imports due to less availability in the country. Most of the stainless steel scrap requirement in the country is met through imports.

This is because there is a very low rate of stainless steel scrap generation given the fact that stainless steel, owing to its corrosion resistant characteristic and high strength, has an extremely long life span (at least 30 years) as compared to any other substitute material. Most of the growth in stainless steel consumption in the country has come about in the last 10-15 years because of which the SS Scrap generation in the country is extremely low.

Stainless steel scrap is the most important raw material required by the stainless steel industry as it is the most cost efficient way of meeting the nickel requirements.

The domestic stainless steel industry uses the environmentally friendly Electric Arc Furnace route (EAF) which necessitates the use of SS Scrap. This technology is perfectly in line with the concept of circular economy and make stainless steel production environmentally sustainable as stainless steel is 100% recyclable material.

The zero duty is required to encourage the stainless steel producers to keep using the EAF route and reduce the carbon footprint of the sector when environment sustainability is becoming an important issue world over.

Major stainless steel producing countries like China, Korea, Japan, EU and USA also have zero import duties on SS Scrap.

3. Increase Basic Customs Duty on stainless steel flat products (7219 and 7220)

Issue

Lower BCD on Stainless Steel flat products (7219 & 7220) vis-à-vis Steel products.

Recommendation

It is recommended to increase Basic Customs Duty on stainless steel flat products (7219 and 7220) from the current level of 7.5% to 12.5% at par with other steel products.

Justification

There is a need for rationalizing these duties due to the following reasons:

Imports have been rising over the last few months. From a monthly average of 34,105 MT in 2020-21, imports grew by an overwhelming 127% in July 2021 and stood at 77,337 MT. This is because of the low customs duty at 7.5%.

These high imports are hurting the domestic industry which has a capacity and capability to meet the entire domestic demand. There is no need of depending on stainless steel imports as the domestic industry can produce all the grades and thicknesses required by the end users. The domestic industry has an installed capacity of 5.04 Million Metric Ton (MMT), with current capacity utilization at 78%, there is enough scope for increasing the capacity utilization to meet the entire domestic demand.

This would be a step in right direction towards Atmanirbhar Bharat.

Other Recommendations

1. Retain Export Duty on Chrome Ore @ 30% on ad valorem basis

Export Duty on chrome ore, a finite natural resource, has been imposed with a view to encourage domestic value addition which is in line with the Hon'ble Prime Minister's vision of 'Make in India'. This should be retained as it is not in the country's long term interest to export minerals without any value addition.

2. Abolition of dual charges on mining leases

The Indian Stamp Act, 1899 mandates payment of stamp duty and registration charges while executing a lease deed, but the Mines & Minerals (Development & Regulation Act), 1957 (MMDR) does not provide surface rights which are essential for carrying out mining activity. Hence, this has to be separately acquired and entails payment of stamp duty and registration charges. In line with 'Ease of Doing Business' initiatives, such dual charges may be streamlined.

3. Removal of Customs Duty on Low Ash, Low Phos Metallurgical Coke

Low Ash, Low Phos (LALP) metallurgical coke is an essential input for production of ferro alloys. This is mostly imported as India does not have adequate reserves of metallurgical coal which is the raw material required to produce LALP metallurgical coke; moreover, the phosphorous content is high. Hence, Indian ferro chrome producers are forced to import LALP metallurgical coke. Since comparative product is not available in India, customs duty on LALP metallurgical coke may kindly be removed.