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PRE-BUDGET MEMORANDUM 2018-19

INDEX

Topic	Page No.
PREAMBLE	4
ECONOMIC OVERVIEW	7
SECTORAL ISSUES	18
– AGRICULTURE	18
– CEMENT	22
– CHEMICALS AND PETROCHEMICALS	23
– CIGARETTES	31
– CIVIL AVIATION	32
– EDUCATION	32
– FINANCIAL SERVICES	35
– FOOD PROCESSING	45
– HEALTHCARE, MEDICAL EQUIPMENTS AND DEVICES	46
– HOUSING & REAL ESTATE	54
– HYDROCARBON	55
– INFORMATION TECHNOLOGY (IT) AND TELECOMMUNICATIONS	65
– INFRASTRUCTURE	67
– MANUFACTURING – CAPITAL GOODS, ELECTRONICS AND CONSUMER DURABLES	69
– MEDIA AND ENTERTAINMENT	75
– MSMEs	76
– NON FERROUS METALS	78
– POWER	83
– PUBLISHING	84
– PULP, PAPER AND PAPER BOARD	84
– RENEWABLE ENERGY	88
– STEEL AND OTHER FERROUS PRODUCTS	90

– TEXTILES	93
DIRECT TAX	96
– Tax Rates – Companies/Firms/Limited Liability Partnership	96
– Tax Rates - Individual Taxpayers	97
– Minimum Alternate Tax and Alternate Minimum Tax	98
– Tax Rate for transactions done through mode other cash	103
– Dividend Distribution Tax	104
– Tax on certain Dividends received from Domestic Companies	105
– Deemed Dividend - Section 2(22)(e)	106
– Phasing out of Deductions and Exemptions vis-à-vis industry needs	107
– Income Computation and Disclosure Standards ('ICDS')	108
– Place of Effective Management	109
– Patent Box Regime	111
– Equalisation Levy	114
– Rationalization of provisions of Section 14A and Rule 8D	117
– Issues related to allowability of certain Expenditures, Deductions and Disallowances	119
– General Anti Avoidance Rule - Chapter X-A	125
– Tax Incentives and Benefits	130
– Carry Back of Losses	137
– Deduction under Section 80JJAA of the Act	137
– Issues – Circulars and Notifications	138
– Non-Resident related provisions	142
– Mergers & Acquisitions	156
– Capital Gains	171
– Transfer Pricing	172
– Financial Services	183
– Tax Deducted at Source (TDS)	187
– Personal Tax	196
– Other Direct Tax provisions	207

INDIRECT TAXES	226
– Goods and Services Tax (GST) - Law and Procedures Related Issues	226
– Customs	253

PREAMBLE

The past year has witnessed several important systemic changes being implemented in the Indian economy. The introduction of the Goods and Services Tax is by far the most important of these, and despite some transitional challenges, this will pave the way for modernizing the Indian tax landscape. We also commend the Government's efforts in seeking to expand the country's tax base, and believe that measures towards this end will help boost our tax-GDP ratio and help increase spending on the social sector.

Tax policy is a key element of our nation's economic reform agenda, and can be effectively leveraged to spur consumption, growth and investor sentiment. The fact that India jumped 30 places in *Ease of Doing Business* rankings released by the World Bank (including a massive 53 places jump from 172 to 119 in *ease of paying taxes* category) speaks volumes of the reforms undertaken by the Government on the tax front. With GST now in force, one can expect these rankings to further improve in the years to come.

Further specific suggestions on the direct and indirect tax side for the consideration of the Government are set out in this Memorandum. We have however taken the liberty of highlighting a few important conceptual issues below that need to be tackled on priority:

1.1. Addressing tax abuse

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 the industry. The most serious of these relate to the newly introduced sections 56(2)(x) and 50CA of the Income-tax Act, 1961 ('the Act'). 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. 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 or suitably relaxed.

1.2. Disallowances under section 14A

Disputes around section 14A of the Act are extremely frequent, and on the increase. The Law Commission, in its recent report stated that the Income Tax Appellate Tribunal had a staggering 91,538 pending cases at the end of 2016. As per the report of the Income-tax Simplification Committee headed by Justice R.V. Easwar, around 15% of the total tax

litigation in the country revolves around section 14A disallowances. For instance, any company earning dividend income or having made any equity investments is, in most of the cases, subjected to section 14A disallowances. Making section 14A inapplicable for dividend income which has already been subjected to Dividend Distribution Tax is, in our view, a fair ask which also aligns to principles of economic taxation. Merely because such income is exempt in the hands of the shareholder does not make it an "exempt income" for the purposes for which section 14A of the Act was enacted as tax on the same is already paid by the dividend distributing company. We therefore submit that section 14A of the Act should be suitably amended retroactively to reflect the above. This will certainly go a long way in putting a much-needed end to the spate of litigation going around on this issue.

1.3. Grant of tax reliefs/concessions pursuant to proceedings under Insolvency and Bankruptcy Code, 2016

The enactment of Insolvency and Bankruptcy Code, 2016 ('IBC') ushers in a paradigm shift in the manner in which insolvency proceedings are carried out in India. Tax considerations also play a vital role in successful implementation of insolvency schemes and hence its significance in the entire gamut of things should not be underestimated. It is thus imperative to ensure that tax consequences do not act as a deterrent in achieving the policy objectives of IBC. As per a recent report, the stressed assets in the Indian banking system have peaked ~ US$ 150 billion (which is approximate to almost 15% of gross advances).

In order to encourage applicants for submitting and implementing viable resolution plans for revival of stressed assets and to achieve the objectives of IBC, it is necessary that certain modifications be made to the Income-tax law in order to ensure that the implementation of Resolution Plans under the IBC does not lead to undue tax costs. In this regard, non-applicability of Minimum Alternate Tax ('MAT') on write back of notional income and non-applicability of section 50CA and section 56(2)(x) on issue and transfer of assets as per the Resolution Plan approved under IBC are vital issues which merit attention. These carve outs are also warranted because the entire proceedings under the IBC are conducted through a transparent process with sufficient regulatory oversight as that of National Company Law Tribunal and hence they do not fall within the mischief which is sought to be curbed by provisions of section 50CA and section 56(2)(x) of the Act.

1.4. Reduce Compliance under GST - A way forward to simplified tax regime

The implementation of GST in the country has been the biggest tax reform that had taken place since independence. We acknowledge and applaud the consistent measures taken by the Government to address the concerns of the taxpayers on this new regime since its implementation. However, the architecture of compliance under the GST regime is in itself a bit complex for instance requirement of invoice level details, matching concept, filing of three returns in a month with plethora of details to be filled in, filing of letter of undertaking in case of exports etc. It is believed that there is a need to review the documentation and compliance related processes by the Government and make suitable changes after due consultation with the stakeholders. The reduced compliance would lead to a simplified tax regime entailing higher compliance.

1.5. Converge to fewer GST rates and include all sectors under its ambit

There is a need to converge the existing band of GST rates to three in line with international standards. Further, to make the GST reform truly effective, all sectors should be within the ambit of GST. Therefore, all excluded sectors / items must be brought under the GST framework.

1.6. Review of Ambiguous Provisions in the GST Laws

It has been observed that certain provisions in the GST laws have created a room for ambiguity and need a re-look by the Government. For example applicability of GST in case of transactions between head office and its branches and consequently issues pertaining to valuation, applicability of GST on transactions between employer and employee, absence of clarity on refund of input tax credit in case of inverted GST structure due to input services etc. It is requested that the provisions of the GST law may be re-examined and ambiguities arising therefrom may be removed by suitable amendments and providing appropriate clarifications, wherever necessary.

1.7. Remove restrictions on claim of Input Tax Credit

Section 17 of the CGST Act, 2017 prescribes certain expenditure in respect of which input tax credit is not available. As a result, the basic objective of introduction of GST intended to remove cascading effect by facilitating seamless flow of credit of tax paid on supply of goods and services at every stage of the supply chain is defeated. It is believed that the provisions in the GST law restricting the allowability of input tax credit on the genuine business expenditure leads to adversity of undesirable cost cascading effect. It is accordingly requested that suitable amendment in the GST law be made to facilitate seamless flow of input tax credit on all expenses incurred for business purpose.

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

1.8. Provide the roadmap for reduction in Corporate Tax rate

In the Union Budget 2015-16, Finance minister proposed to cut the corporate tax from 30% to 25% over four year period ending 2018-19, along with removal of exemptions. As of date, the corporate tax rate has been reduced to 25% only for companies with annual turnover upto Rs 50 crore. There is a need to bring down the corporate tax rate for other companies as well and a roadmap should be provided in this respect. The cut in corporate tax rate can in-fact have positive effects on tax revenues owing to expansion of tax base. This has been proven in countries like Russia and Turkey.

ECONOMIC OVERVIEW

2.1. State of global economy

- 2017 marks ten years of one of the worst financial crisis that hit the global economy. The economic consequences of the crisis reverberated across the world with GDP growth plunging across geographies and calls for reforming the global financial system getting stronger. The crisis triggered a coordinated response from the countries and today the global economy has been able to recover from the turmoil that followed. The latest IMF World Economic Outlook released in October 2017 reports strengthening of global growth. Growth is projected at 3.6% and 3.7% in 2017 and 2018 respectively. There are indications of a pickup in investment and industrial activity; and trade performance is also gaining strength. The recovery in advanced economies (being supported by the Euro Area) and a few other large emerging economies (China) is gathering steam. In-fact, better growth prospects in the Euro-zone, Japan and China have compensated for relatively lower growth in the US, the UK and India.
- The demand conditions are seen improving in the advanced economies. According to the IMF outlook, Euro Area is expected to grow by 2.1% in 2017 and 1.9% in 2018. Further, the business and consumer confidence in the United States has been buoyant and the country is expected to expand by 2.2% in 2017. In Japan too, growth momentum is seen remaining intact with expanding trade and government's fiscal support.
- With regard to emerging market and developing economies, the recovery is gradually shaping up but continues to remain dispersed. Growth in China is improving and the country is focusing on structural reforms. Other countries such as Brazil, Mexico, Russia and Turkey are also witnessing some consolidation in terms of their growth performance.
- Nonetheless, growth is yet to fully firm up and there are some downside risks that can mar the growth prospects.
- Even though the recovery in US market continues, but its better growth is largely dependent on the passage of tax reforms and moderation in rise of interest rates. Secondly, global trade has seen recovery this year and even though the threat of protectionism has lowered, uncertainty remains which could halt further improvement in global trade. The high levels of debt afflicting the Chinese economy also merit close attention. The factor that could have a drastic impact on global growth is the geo-political conflict, especially in North Asia and Middle East. Further tension in this region could elevate energy prices and lower equity markets, thereby impacting overall recovery.

2.2. State of Indian economy

- Indian economy has largely exhibited resilience to the global economic conditions on the back of growing domestic economy. India's GDP growth averaged about 7.5% between the years 2014-15 and 2016-17. However, GDP growth in quarter 1 of 2017-18 moderated to 5.7% - which was the lowest in about 13 quarters. This was primarily due

to adjustment impact of key structural reforms, especially the demonetisation move in November, 2016 and the implementation of Goods and Services Tax from July this year that caused supply disruptions. However, these disruptions are only transient and expected to ease out over the next few quarters. Already the numbers for quarter 2 of 2017-18 show that the economy is on a recovery mode with growth climbing up to 6.3%. Over the long term, GST will have a positive effect on the overall health of India's economy, especially when accompanied by further reforms.

- The slowdown in the initial months of the current year is also reflected in the performance of the Index of Industrial Production (IIP). For the period April-September 2017, the IIP index observed 2.5% growth, which was lower than 5.8% growth witnessed during the same period last year. The informal sector and small & medium enterprises were adversely hit due to demonetisation and this was aggravated by the initial compliance hurdles emanating from GST introduction. There is a need to take measures to provide support and incentives to such informal and small enterprises to aid their revival and growth.
- There is a likelihood that demonetisation effects may linger on for some more months and hence there is a need to further boost demand. The Government should consider revision of income tax slabs, by raising the income level on which peak tax rate would trigger. This would improve purchasing power and create additional demand. For individual taxpayers, 30% tax rate should be applicable only if the income is above Rs 20 lakh. Additionally, interest rates should be lowered to enable affordable finance for conducting business operation and expansion.
- The recent adjustments in the GST tax rates are noteworthy and will help in lowering of prices, thus supporting overall demand. Further rationalisation and simplification of GST rates should be pursued. FICCI has been recommending inclusion of all sectors under the ambit of GST and convergence to 3-4 GST rates.
- There has been some improvement in demand over the last few months. Some lead indicators point towards signs of recovery in industrial activity. Air passenger traffic and air freight growth remains in the double digit terrain. Further, the IPO activity this year has been encouraging. Also, the latest NIKKEI India manufacturing PMI has reported an improvement. The industry is beginning to tide-over the transition issues related to GST and production schedules are now getting normalized.
- The challenging issue however is the private domestic investment cycle that continues to remain weak. Corporate investment has slowed down from a peak of 15% of GDP in 2007-08 to around 11% of GDP since then. Domestic production has been affected by significant rise in imports on the back of concessional entry under various FTAs as well as substantial appreciation in the Rupee. In the last three years, India's real exchange rate has become overvalued on the back of high domestic interest rates that have attracted huge capital inflows. A reduction in repo rate, combined with effective transmission into lending rates will help in moderating capital inflows and reducing Rupee appreciation. A recovery in private sector capex is probably a year away.

- The government should also take reform measures to improve competitiveness of Indian industry. The New Industrial Policy of the government should incorporate specific measures in this regard. Focused reforms on doing business have helped India move up the rankings on Ease of Doing Business by 30 places to 100th position. Similar focused efforts are required to improve the cost of doing business, which directly impacts the competitiveness of Indian industry. Specifically, there is a need to pursue the land, labour and energy sector reforms with greater vigour.
- The slowdown in private investments is corroborated by the slowing credit growth to the private sector. The change in real credit to the private sector which earlier was over 10% of GDP has slowed down to under 5% of GDP. Even though the latest monthly non-food credit numbers have reported an uptick, the offtake is yet to reach the pace to put the growth cycle in full motion. The twin balance sheet problem – overleveraged corporate balance sheets and bad loans on bank balance sheets - has been deterring investment revival. The gross non-performing assets crossed Rs 8 lakh crore in the quarter ending June 2017. The gross NPA's are even higher if restructured assets are included. The problem is bigger in public sector banks but even in private banks, the NPA ratio has been rising.
- The government and the RBI have indeed taken steps towards banking reforms, especially focusing on the four R's: recognition, resolution, recapitalisation and reform. Since 2014, the RBI has been proactively forcing recognition of the problem. The introduction of Insolvency and Bankruptcy Code 2016 has enabled mechanism for faster resolution. In terms of recapitalisation, the government announced Indradhanush Scheme in 2015 and the latest recapitalisation scheme of Rs 2.11 lakh crore is a welcome step. However, the recapitalisation plan must be accompanied (even preceded) by reforms in the banking sector. One of the performance criteria the management of the banks must agree to before recapitalisation is the new lending targets.
- There has been a move towards bank consolidation as well, beginning with the measure of merger of SBI with its associate banks. These measures have been in the right direction and need to be implemented completely. There is ample scope for further consolidation and even privatisation of some of the public sector banks, having at the most 5-6 large public sector banks.
- In addition to the credit slowdown in corporate sector, slowdown in investments can also be attributed to the slowing household investments. The contribution of household sector to gross fixed capital formation has steadily declined from 46% in FY12 to 37% in FY16. In y-o-y terms too, household investments have remained weak, registering decline in FY13, FY14 as well as FY16. One of the reasons for same could be slower job creation and slow pace of increase in disposable incomes in recent years.
- It is thus recommended that the Budget should continue to lay thrust on boosting consumption and investments, by way of revision in tax slabs, lowering of interest rates as well as providing incentives for investment in housing.

- The recent stimulus plan introduced by the government also includes a new umbrella Road Building Project with an estimated capex of Rs 6.92 lakh crore to be spend over the next five years. Out of this, Bharatmala Pariyojana (for road and highways development) is to be implemented with an outlay of Rs. 5,35,000 crores and is likely to generate 14.2 crores man-days of jobs. The scheme targets to build over 83,000 kms of roads.
- The infrastructure sector has significant backward and forward linkages and the Government's focus on this sector is noteworthy. Government has been giving a strong impetus to development of all areas of infrastructure be it roads and highways, railways, airports as well as waterways and this must continue. The increase in public expenditure on infrastructure projects will also crowd in private investments and eventually support growth and job creation.
- To ensure effective implementation of the ambitious infrastructure development plans and facilitate private sector participation in same, it is important that the Government addresses the concerns related to financing of PPP projects. Even for the proposed Bharatmala road project worth Rs 5.35 lakh crore, nearly Rs 1.05 lakh crore of the investments will have to come from private financing and it is critical to ensure that problems experienced in the past do not recur. The hitherto problems in PPP projects have occurred due to inadequate understanding and attribution of risks in these projects to lack of sectoral flexibility in their design. The Government should consider recommendations made by the Kelkar Committee in addressing these issues, especially by establishment of a 3Pi an institute or body to guide future development of PPP projects in India.
- On the inflation front, both wholesale and retail prices have remained range bound. The consumer price index, which has been chosen as the key measure of inflation by RBI for policy purposes, averaged 2.7% over the period April- October 2017. The corresponding number was 5.2% over the same period last year. Food and beverages prices (particularly pulses, egg, meat, fish and sugar prices) which were a key pressure point until last year have softened and the overall prices remain within RBI's indicative trajectory of 4.0%.
- While RBI has been following inflation targeting framework in devising its monetary policy, it has been observed that its projections have been persistently wrong for the last two years, resulting in significantly higher interest rates. In India, inflation is largely driven by imported commodity prices and / or by food prices. The inflation targeting framework is counter-productive in dealing with this type of inflation as it exacerbates the problem even further by keeping real interest rates too high. As such, there is a need to review the framework by an independent panel.
- India also needs a pro-active trade policy for essential food items to manage price surges including buying options in futures markets.
- Adequate food stock and effective supply management will also help keep a check on food prices. There is a need to double up efforts to boost agri-production and agri-productivity as well as improve the distribution and supply chains. Steps taken for

agriculture market reforms including the APMC act and e-NAM initiatives are noteworthy and need to be implemented rigorously. The Government's plan to link various agro-processing clusters with the production centres through Mega Food parks is also a welcome step.

- On the external front, India's merchandise exports increased by 9.0% over the period April to October 2017 as compared to 0.1% growth reported over the corresponding period last year. The improvement in external demand conditions is supporting India's exports. In fact, our cumulative exports to major destinations like Americas and Asia noted an increase during the first five months of the fiscal year 2017-18. Imports too observed 22.9% growth over the period April-October 2017 as compared to (-)10.1% growth reported over the same period previous year. Besides the rise in oil import bill following rise in oil prices, high levels of import of gold and silver have majorly contributed to this spike in growth. The appreciating Rupee has also contributed to the increase in imports. India's merchandise trade deficit has seen an increase in recent times and we also see the deficit on the current account inching up to 2.4% in the first quarter of 2017-18. Rising oil prices are worrisome external risks and the terms of trade for India will be adverse. The rising oil prices could inflate India's oil import bill going forward, putting some pressure on balance of payments. Nevertheless, it is expected that robust capital inflows and healthy forex reserves will help in managing the balance of payments.

- Lowering the RBI's repo rate and ensuring quicker pass-through of RBI rate cuts by the banks to consumers would help moderate capital inflows and reduce the Rupee appreciation which is hurting domestic industry. There is also a need to review the existing FTAs, especially India-ASEAN FTA, which has resulted in growing deficit with ASEAN countries. Similarly, India's trade deficit with China has ballooned over the years, especially for electronic goods. There is a need to ensure that trade with China has a level playing field, thereby restricting dumping of China's subsidized exports in India.

- Foreign direct investment inflows have been robust. The reform oriented approach of the Government and various steps taken towards improving ease of doing business and liberalising the FDI regime have supported inflows. According to DIPP, provisional estimates for 2016-17 show foreign direct investment inflows at US$ 60.1 billion vis-a-vis inflows worth US$ 55.5 billion in 2015-16. Direct investment inflows up to September this year have been US$ 33.7 billion. However, much of the FDI into India serves the domestic market. There is a need to push for export-oriented FDI as well so that India not only becomes an export hub but also an integral part of the global supply chains.

- Further, India's foreign exchange reserves stood at an all time high of USD 400.7 billion at end of November, 2017 – providing an import cover for about 12 months.

- The fiscal deficit to GDP ratio for 2017-18 has been pegged at 3.2%. Following demonetization, the concomitant emphasis on digitization and implementation of GST, there has been a large addition to the tax payers base in the country.

- However, there are three main concerns for achievement of this fiscal deficit target. First of all, following the demonetisation drive, RBI's dividend to the government is much lower than the previous year, primarily owing to the cost incurred by the central bank in printing of new currency notes and in sterilisation of excess liquidity. Second, the rising oil prices will make it difficult for the government to earn windfall gains from tax revenues like it did in the previous year, when oil prices were on a decline. Third, even though the government has been able to generate adequate revenue from the GST so far, the slow economic growth could impact direct tax collections. The recent lowering of GST rates on several products will also have revenue implications.
- Additionally, the Union budget will need to absorb the additional costs of the fiscal stimulus plan for road infrastructure and bank recapitalisation announced recently. While such public capex is important to push growth, it may put burden on the fiscal. With deteriorating finances at the state level the scope for relaxation is limited if any without risking a down-grade. The Government should thus focus on rationalisation of revenue expenditure, especially through the wider expansion of direct benefit transfer for all subsidies. If needed, the Government should consider monetizing its developed infrastructure assets/ idle assets of PSUs to raise more resources, and accelerate privatisation.

Some major reforms / program announced / implemented in 2017-18

Banking Regulation (Amendment) Bill 2017	The Banking Regulation (Amendment) Bill 2017 was passed in the Parliament in August this year. The Government can now also authorize RBI to direct banks to initiate insolvency proceedings against defaulters under the Insolvency and Bankruptcy Law. This is a major step and together with Bankruptcy law, it will help in resolving the NPA problem in time bound manner.
Real Estate Regulation Act	The Act which was passed in the Parliament in 2016 came in to force from May, 2017. RERA is expected to bring transparency and improved governance in real estate dealings and will reduce the litigations going forward.
Goods & Services Tax	Goods & Services Tax implemented from July 1, 2017. GST will create a unified market making Indian industry more competitive and will contribute significantly to growth of economy in the medium to long term.

Saubhagaya Yojana	Prime Minister launched Saubhagya Yojana on 25th September, 2017. The objective of the Saubhagya Yojana is to provide energy access to all by last mile connectivity and electricity connections to all remaining un-electrified households in rural as well as urban areas to achieve universal household electrification in the country.
Bank Recapitalisation	Rs. 2,11,000 crore Bank Recapitalisation plan announced to help banks meet the BASEL III requirements, address the NPA related problems as well as have greater capital for pushing credit growth
Bharatmala Pariyojana	This Road Building Program for 83,677 km of roads involves capex of Rs.6.92 lakhs crores over next 5 years. The project will give a massive thrust to infrastructure development in the country and will also crowd in private investments.
Bank Consolidation	Cabinet has given an in principle approval to the framework for consolidation of banks. SBI merged five of its associate banks and Bharatiya Mahila Bank with itself earlier this year. India needs to have large banks that can support investment needs and support economic growth.
Strategic Disinvestment of PSUs	The government has invited bids for strategic disinvestment in identified CPSEs. Once completed, this will help improve the growth prospects of these companies.

2.3. Summary of Key suggestions for Union Budget 2018-19 for promoting growth

After a blip in growth as seen during the first quarter of the current fiscal, Indian economy has started seeing an improvement in performance and the recently announced measures particularly those related to the banking sector and public expenditure in the infrastructure sector should help improve this momentum. The reform process should continue and the forthcoming Union Budget should focus on stimulating investments, boosting demand, rationalizing taxes and addressing some of the key policy hurdles. Some of the suggestions for consideration of the government are provided below.

2.3.1. Macro-economic suggestions

- The Government should continue laying strong emphasis on capital investments. Public spending on infrastructure and social sector should be kept up to stimulate growth. This may require slight calibration of fiscal deficit target. If limiting the consumptive expenditure and promoting productive expenditure that adds to the overall capacity of the economy leads to some increase in the fiscal deficit, this should be considered. Further, the government can **consider monetizing its developed infrastructure assets/ idle assets of PSUs** to raise more resources.
- There is a need to **expedite strategic disinvestment of public sector enterprises** to raise non-tax revenues for funding various development expenditures. Announce a ten year plan for all public sector enterprises with respect to their ownership, disinvestment, labour management, and utility of proceeds, etc. The resources raised from such disinvestment can be set aside into the National Infrastructure Investment Fund, which can then be leveraged to attract more private investment into a common fund.
- Government should also **consider privatization of public sector ports** to bring efficiency in operations. Alternatively, long term lease arrangements for private sector may be considered for port-led development.
- There is a need to **lower the cost of finance for industry** – large as well as MSMEs – which is currently very high. As per FICCI's Business Confidence Survey, the average lending rates of banks are around 12%. The RBI should consider cutting policy rates by at least 100 bps. Government should work in tandem with RBI to enable reduction in policy and lending rates, which is desired to propel demand for interest sensitive sectors such as consumer durables, auto and housing. Lower interest rates will also help in having a competitive exchange rate, which is essential for growth of domestic industry.
- A quick and independent review of the monetary policy framework and its implementation is needed. The monetary policy transmission needs to be strengthened.
- The Direct Benefit Transfer scheme should be further expanded to include all subsidies, as they are better targeted and can also reduce leakages thereby releasing funds for social and physical infrastructure.

2.3.2. Tax reforms and measures

- The Government has been very responsive to industry's concerns related to GST. It should **continue to address all pending issues related to implementation of GST**, especially to ease the compliance requirements related to GST for MSMEs.
- Additionally, there is a need to **fast track convergence to fewer GST rates. There is a need to move towards three rates in line with the international best practices.**
- To make the **GST** reforms truly effective, **all excluded items must be brought under the ambit of GST.**

2.3.3. Banking sector reforms

- After the consolidation of SBI with its subsidiaries, the government should now **consider consolidation of other public-sector banks** to create globally sized banks and bring in efficiency.
- The government should also **consider divesting its stake in the public-sector banks to enable banks to raise capital from the market.** Government can look at having 26% share as a floor and bring in the concept of a golden share to exercise control over critical decisions.
- There is a **need to** establish **a Development Financial Institution** for Industry, especially focusing on large scale projects like infrastructure.

2.3.4. Factor Market Reforms

- Land acquisition for business activity remains an issue. Surplus land along rail lines and stations, land along major transport corridors, housing schemes, could be set aside for commercial activity.
- A simplification and rationalization of multiple labour laws into 4 codes was announced in last year's Union Budget. This should be completed and the Government should ensure that the framework of labour laws puts in place adequate flexibility for enterprises, while incorporating appropriate safety and security net for the workers. At the same time, more States should be encouraged to undertake labour reforms.

2.3.5. Enhancing access to finance for MSMEs

- **Promote trade receivables and discounting systems (TReDS)** amongst MSMEs through planned marketing campaign. Additionally, provide incentive on usage of TReDS platform.
- Government can also consider **creating an** insurance **scheme for receivables financed on TReDS**.
- **Encourage wider participation on TReDS platform**. While the government has recently announced that PSUs will have to register on TReDS, larger NBFCs may also be encouraged to register on the TReDS platform as this will make the platform even more active.

2.3.6. Regulatory review and reforms

- There is a scope for further **improvement in functioning of key regulators** through measures such as capacity building and regular industry interaction.
- **Various parallel regulatory approval processes by multiple regulators should be minimized** to ensure that business activities are not hindered due to lack of co-ordination between various regulators or cumbersome procedural formalities. Currently, several regulatory agencies have over-lapping jurisdiction, leading to duplication and over-regulation. A regulatory review with consultation and co-operation from commerce and industry associations should be done to avoid duplication and over-regulation.

2.3.7. Stimuli for greater investments and expansion

- The government can **consider establishing Regulation Free Zones**, wherein all regulatory requirements, except those for national security and health, can be relaxed. This can be done to encourage establishment of new-age, high-technology and innovative industries. These may also be considered in conjunction with port-led development plans of the Government. To start with, the Government may consider 2 or 3 such zones.
- **Special impetus needs to be continued for certain key sectors like housing** as these can have a multiplier effect on demand creation across industries. There is also a need to address policy bottlenecks in some specific sectors such as Steel, Cement and Power, while simultaneously giving them a growth thrust through supportive policy measures. Continuous thrust on affordable housing segment is also required to encourage greater household investments, which have remained subdued over the last few years.
- There is a need to give added impetus to the innovation culture in the country, as improved productivity through innovation can aid in attaining faster growth. **India must have a comprehensive program for innovation on the lines on 'Make in India' initiative.**

2.3.8. Foreign trade and investments

- Specific policy measures may be introduced to increase exports of Indian companies. For instance, government may **consider extending special incentive package schemes introduced for textiles and leather sector to other export items as well**.
- The skewed balance towards imports needs to be corrected to encourage fresh investments by domestic companies. This requires a **complete review of existing FTAs and exercising due care while entering into any new FTAs, ensuring that it leads to effective market access for Indian companies.**
- **The incidences of inverted duty structure should be corrected to provide level playing field to domestic industry**. This is important as some cases of inverted duty structure continue, especially in sectors like Capital Goods, Electronics and Electricals, Metals & Minerals, Textiles and Tyres. Cases of inverted duty structure resulting from GST also need to be addressed.

2.3.9. Enhance digital transactions

- Introduce **steps to dicentivise use of cash**. For instance, RBI can prescribe mandatory Cash Handling Charges (CHC) for current accounts of all banks above a particular threshold.
- **Rewards / incentives scheme should be introduced for merchants as well as consumers for doing digital transactions**. For instance, tax rebates can be given for merchants as well as consumers in the form of lower GST rates for digital transactions. Likewise, other surcharges and levies on digital transaction can be reduced / waived off.

- Provide **incentive to promote domestic manufacturing of POS machine**, which can be made available with merchants at lower costs.
- Work towards **greater integration of various digital platforms**, by allowing inter-operability amongst banks, card networks, and non-banks payment systems.
- **Create a 'grievance redressal mechanism' for digital payments** viz. 24 x 7 call centre, helpline, website, etc.

2.3.10. Encourage formalization of economy

- For small **entrepreneurs** up to a specific threshold of turnover, the government can **consider introducing a scheme of 'one tax / one pay'**, wherein all types of taxes and levies (corporate tax, GST, social security, property tax, etc.) are removed and one single payment is made on annual basis.
- Often, non-**compliance** to various labour, environmental regulations by small enterprises happens due to lack of knowledge of the regulations. In order to encourage enterprises to formalize, the government may **consider replacing penalty / fines in case of first non-compliance with training and workshops**.
- While the Udyog Aadhar Memorandum (UAM) has simplified MSME registration, the government may further **consider linking all possible clearances and licenses within UAM** itself, so that enterprises can close all formalities in one go.
- Revise the existing definition of MSMEs to include turnover/ employment criteria and have a mechanism to revise the same every three years.
- The government should **facilitate setting up of 'Business Support Centres'** (probably within the District Industries Centres) to assist MSME registration, responding to all their queries, resolving their doubts and assisting them in complying with all processes.

SECTORAL ISSUES

AGRICULTURE

Goods and Services Tax (GST)

3.1.1. Agricultural Machinery

Since independence, agriculture and agricultural machinery has been kept out of all kind of taxation for the benefit of the farmers. Before the GST regime, there was no Excise, no VAT (except in same states) and no other levies, on the agriculture inputs especially, agricultural machinery. This was done by the government to keep the prices of agricultural machinery affordable for the farmers to encourage them, to go for mechanization of various farming operations in their field. It is pointed out that mechanization is a key area of agriculture and high rates of GST will dissuade farmers to go for mechanization, which may result in decrease in crop production. High rate of GST will cause a negative effect on the adoption of agricultural machinery. It is suggested that rate of GST on agricultural machinery may be reduced to 5% instead of presently 12%.

3.1.2. Ambiguity over rate of GST

There is a lot of confusion in the industry about the exact rate of GST on various kinds of implements, as well as on the parts used for the manufacturing of agricultural machinery. Some of the issues for consideration as well as clarification from the Government are given as below:-

3.1.3. GST on hand operated and animal drawn Agricultural Implements

The GST Council had approved nil rate for agricultural implements manually operated or animal driven covered under code HSN 8201. However, the manufacturers of some of the manually operated agricultural implements such as manual chaff cutter, manual sprayer very basic machines in agriculture and used by small and marginal farmers, are not clear whether the machine would be covered under this code. It is accordingly requested that a clarification may be issued to provide that all manual and animal drawn agricultural implements and their parts shall be covered under HSN code 8201and would be subject to GST at nil rate.

3.1.4. GST on Power operated Agricultural Machinery

There is 12% GST on complete agricultural machinery, however there is no mention of parts in the HSN code details, due to which there is utter confusion in industry on the GST rate applicable on the various kind of parts used in the manufacture of power operated agricultural machinery. On perusal of the HSN codes of GST, either the parts are mentioned in description of goods or separately mentioned under separate HSN code, but are clearly mentioned. Some of the examples in this regard are given below:-

HSN code	Description of goods	GST
8437	Machines for cleaning, sorting or grading, seed, grain or dried leguminous vegetables; machinery used in milling	5%

	industry or for the working of cereals or dried leguminous vegetables other than farm type machinery **"and parts thereof"**	
8431	Parts suitable for use solely or principally with the machinery of headings 8425 to 8430	18%
8466	Parts and accessories suitable for use solely or principally with the machines of headings 8456 to 8465 including work or tool holders, self-opening die heads, dividing heads and other special attachments for the machines; tool holders for any type of tool, for working in the hand	18% (8456 to 8465 all under 18%)
8503	Parts suitable for use solely or principally with the machines of heading 8501 or 8502	18% (same as of 8501, 8502)
8538	Parts suitable for use solely or principally with the apparatus of heading 8535, 8536 or 8537	18% (same as of 8535, 8536, 8537)

The above, parts suitable for use solely or principally with machines are covered under the same rate of GST or lower than the GST rate applicable on the machines. It is thereby requested that parts of agricultural machinery shall be covered under same GST rate. For this purpose either "parts thereof" shall be added in the description of goods under HSN codes 8201, 8432 and 8433 or a new HSN code covering parts of agricultural machinery may be created stating "All parts for use solely or principally with the machines of heading 8201, 8432, 8433" and the GST rate applicable shall be nil or 12%, same as that of complete machines.

3.1.5. GST on Sprayers

Pre GST taxation regime, the manual Sprayers, which are mostly used by small and marginal farmers, were subject to nil rate of tax. The Government has announced that all manual and animal drawn agricultural machinery will be subject to nil rate under GST. However, under GST tariff, it is being covered under 8424 subject to tax at the rate of 18% and the description of goods says:

"Mechanical appliances (whether or not hand-operated) for projecting, dispersing or spraying liquids or powders; fire extinguishers, whether or not charged; spray guns and similar appliances; steam or sand blasting machines and similar jet projecting machines [other than and Nozzles for drip irrigation equipment or nozzles for sprinklers]

It is requested that a clarification may be issued to provide that manual sprayers will be subject to nil rate of GST classified under HSN code 8201. It is further suggested that all other kind of sprayers such as power sprayers, tractor operated sprayers, mist blowers may be covered under 12% GST.

3.1.6. GST on Brush cutters, Power Weeder and Chain saw

The brush cutter is a hand held machine using power for its operation. Its use is both in agriculture and horticulture. It is largely used for crop harvesting by farmers. Power Weeder is a hand held machine using power for weeding operation in crops, plantations etc. Chain saw is a machine, which is a power operated tool used in forestry in place of manual wood cutting saw. Principally all the three machines are used in agriculture, horticulture and forestry. Accordingly, Power Weeder shall be covered under HSN codes 8432 and Brush cutters and chain saw shall be covered under HSN code 8433. However, there is ambiguity prevailing in the industry with regard to its classification and the same is being classified under HSN code 8467:-

"*Tools for working in the hand, pneumatic, hydraulic or with self-contained electric or non-electric motor"*

The HSN code 8467 is for any kind of mechanical tool which may be used in any industry as there are separate codes for agricultural purpose and in this description, agriculture, horticulture or forestry is not mentioned. So, Brush cutter, Power weeder and Chain saw shall not be classified under this HSN code.

It is requested that clarification may be issued that Brush cutter, Power weeder and chain saw shall be covered under HSN codes for agricultural machinery i.e. 8432 and 8433.

3.1.7. Updating HSN codes for covering all kind of agricultural machinery

The HSN codes under GST are based on the Excise duty codes which are very old and have not been update since long. A lot of new kind of agricultural machines have been developed and are used by farmers. There is a need to update the old codes and create new codes for these latest machines. It is suggested that a mechanism may be evolved to do so and list of latest agricultural machinery for updating the existing codes to accommodate all new kind of agricultural machinery may be requested from the industry.

3.1.8. Tax on input services in relation to storage and warehousing of agricultural produce

Under the GST regime, the services in relation to agricultural produce inter-alia services by way of post-harvest storage, infrastructure for agricultural produce including cold storages is exempt under GST. However, the service of renting out of immovable property for storage of agricultural produce is liable to GST. Thus it becomes a cost to a registered entity since the output supply i.e. service of storage and warehousing of agricultural produce is exempt from GST. Such service provider therefore would not be entitled for any input credit and therefore, the cost has to be passed on which in turn would increase the cost of the agricultural produce. The non-availability of input credit may also result in corresponding deduction in the price of the produce being paid to the farmers which will only burden the farmers. Thus, by exempting one end of the value chain, i.e. storage of agricultural produce from the ambit of the tax and taxing another leg of the chain, i.e. renting of property for storage of agricultural produce, an unintended anomaly has crept in GST law which defeats the objective of reforms and boost in the agriculture sector through GST. It is suggested that

renting of property for storage of agricultural produce should be exempted from levy of GST.

OTHER ISSUES

3.1.9. Uneven Mandi Tax

Due to different mandi tax structure in different states for the same commodity, an imbalance is created in the inter-state flow of agri-commodities. Thus, non-uniform mandi tax levied by the states goes against the 'one nation one tax' vision of GST. The implication of this variance will have a negative impact on farmer's income and will also create an imbalance in the flow of commodity from one state to another. Hence, a uniform tax across all mandis should be levied. This will also be in-line with the government's initiative of creating electronic linkages across mandis under e-NAM.

3.1.10. WDRA registered Warehouse should allowed to act as e-sub market yard/Private mandi

Presently the farmers are depended on APMC mandis to sell their crops. These mandis are normally situated far from farms which has limitations in terms of increased cost of logistics, multiple times loading and unloading charges, non-availability of warehousing infrastructure and other operational issues. Hence, granting of license of e-submarket yard or private mandi to WDRA registered warehouse will provide ease to farmers to carry goods for selling and help in reduction in cost of loading and unloading as buyer can store spare quantity of the commodities in the warehouses. It will also save the spillage loses and avoid distress sale as farmers may also opt to store commodity in warehouse for some time.

3.1.11. E-market for procurement of commodity through auction – State wise registration

Presently companies providing services of procurement through e-auctions are required to take registration in each state where they wish to operate, which results in increased compliance burden and paper work. The license application and allotment process takes time and documents required are also not standardized across states. This acts as deterrent for companies to carry out activities on pan India basis. Also, it leads to paper auctions and manual intervention which is not transparent. Hence, it is required to grant licenses on pan India basis to companies providing e-auction facilities for buying and selling of commodities. This will also increase market participation and help in fair price discovery of commodities.

3.1.12. Regulations on Usage of Agricultural Drones

Aiming at the betterment of farming community of the country, bringing-in new technologies will ensure this objective. Agricultural drones will play a critical role. Due to lack of clear guidelines, usage of drones is limited. Government is requested to develop usage guidelines as to identify the areas/places where drones should not be used, and promote its usage for the betterment of the agriculture dependent communities at the earliest.

3.1.13. Leverage full potential of e- NAM

The Government boldly put forth the vision of creating a unified national market for agricultural commodities through the launch of the e-NAM initiative in April 2016. Farmers and corporates alike await the unleashing of e-NAM's full potential to provide greater selling choice to farmers and reduce transaction costs and improve quality for buyers. It is therefore suggested that the following steps may be taken in the forthcoming Budget to revitalize e-NAM to ensure the full delivery of its benefits:

For leveraging full potential of e- NAM: following steps may be taken:-

i) Creation of a joint venture company with 50:50 public and private holding and allocation of the mandate to roll out e-NAM to this entity.

ii) Free e-NAM from bondage of APMC market yards.

iii) Enactment of a special legislation under the "trade" entry of the Union List of the Constitution to enable smooth and seamless passage of agri goods traded on e-NAM across State borders.

iv) Cap the fee payable on inter-State transactions on e-NAM at 1% to incentivize large buyers to get onto the platform.

v) Provide a financial incentive to States for the number of e-NAM trading points they facilitate.

3.1.14. Crop Insurance

With PMFBY (Pradhan Mantri Fasal Bima Yojana), Government of India has taken a big step towards insurance of crops. However, for the success of the scheme it is important that state as well as central government should make provision for timely subsidy to insurance companies. This would be important to serve the additional features such as prevented sowing, on account claims and localized claims.

Under PMFBY, the state governments should invest in a series of Automatic weather stations or rain gauges to identify the weather conditions at localized manner. As per few studies, India needs to have one AWS at very 5 km and one ARG at every 2 km or one AWS in every village. This requires considerable investment at state and central level.

CEMENT

3.2.1. Since 2007-08 import of cement into India is freely allowed without having to pay basic customs duty whereas all the major inputs for manufacturing cement such as Limestone, Gypsum, Coal, Pet coke, Packing Bags etc. attract customs duty. Presently due to low demand of cement in the country more than 116 million tons of domestic cement capacity is lying idle and duty free import of cement causes further undue hardship to the Indian cement industry already reeling under low capacity utilization. Therefore, it is requested that to provide a level-playing field, basic customs duty be levied on cement imports into India. Alternatively, Import duties on goods – Coal, petcoke, Tyre Chips, Limestone, Packing Materials & Bags, Gypsum, and Refractories etc. - required for manufacture of cement be abolished and freely allowed without levy of duty.

CHEMICALS AND PETROCHEMICALS

3.3.1. The Indian Chemical Industry is an integral part of Indian economy. The industry has key linkages with several other downstream industries such as agriculture, infrastructure, textiles, food processing etc. Over the last few decades, the chemical industry has seen an increasing shift towards Asia. The Indian chemical industry is estimated to be valued at $147 bn in 2015 and contributes to 3% of the global chemical industry. The industry is one of the most diversified of all industrial sectors covering ~80,000 products.

The growth of this sector will be primarily driven by domestic consumption because per capita consumption of most of the chemicals is much lower than global averages. The government has been taking initiatives to address challenges in infrastructure, feedstock availability, complex tax and duty structure and overcome other system intricacies. One of the initiatives is 'Make In India' campaign, which aims to facilitate investment, foster innovation, enhance skill development and build best-in-class manufacturing infrastructure.

To meet the increasing demand of chemicals, either the local production will have to ramp up or the imports will have to go up. As import duties have fallen across South and Southeast Asia, resulting primarily from FTAs impact, large global manufacturers have set up transnational supply chains in countries with better infrastructure, ports and friendly regulatory regimes. This has led to global players shifting from manufacturing to assembly and, subsequently, to outright imports into India. Our view is that sustained growth is more likely to stem from the rise of domestic manufacturing, rather than relying on international companies. Besides simplifying regulatory processes and compliance related issues, the government will have to look at policies specific to the chemical manufacturing sector to generate sizable impact. Industry feels Free Trade Agreements (FTAs) are having a negative impact on business. FTAs create an 'inverted duty structure' making it cheaper to import a finished product rather than manufacturing or assembling it in India.

The chemical industry continues to face several challenges. Availability of feedstock at competitive cost remains a key concern. Lack of domestic manufacturing of several intermediates increases lead times and lowers competitiveness of downstream producers. Lack of adequate physical infrastructure and sub-par chemical logistics infrastructure makes material production and movement cost intensive. Uninterrupted power supply remains a challenge for the energy intensive chemical industry. To add to above, significant glut in global chemical capacities has led to growth of imports in India. Large capacity additions in Middle East and USA are another cause of concern for the domestic players. The duty structure needs rationalization for several products value chains in order to boost domestic value addition.

3.3.2. Feedstock for Chemical Industry

(a) Reduction of Customs Duty on Feedstock Ethyl Alcohol/Ethanol (HSN 22072000)

In the year 2015-16, estimated molasses based ethanol production was around 250 crore litres against total consumption of around 300 crore litres, where deficit was met through large quantities of imports done by the chemical industry. Launch of Ethanol Blending Programme in the country has resulted in an upsurge in ethanol demand. Latest tender

issued by PSU OMCs for ethanol procurement has come up with a volume requirement of 280 crore litres, with the aim to achieve 10% blending level.

The availability of ethanol has fallen further in the current sugar year 2016-17, where sugar production is down by 20%. This has resulted in very limited ethanol availability to chemical industries. Due to the inadequate supplies of ethanol in the domestic market, Indian Chemical industry is forced to import ethanol. In the past five year, ethanol has been continuously imported and with the existing scenario, the chemical industry would be dependent on ethanol imports for its major requirement.

On application side, the downstream applications of ethanol are fuel blending, potable liquor, Pyridine, Mono Ethyl Glycol (MEG- further used for Polyester Fiber and Films, Packaging Films and Pet bottles etc.). Ethyl Alcohol is also used for making Acetic Acid, Ethyl Acetate and Acetic Anhydride. Most of these products (Pyridine, Ethyl Acetate etc.) are exported out of country and are major building block for various agro chemicals and pharmaceuticals products. Removal of Duty will further boost the export of such products and will increase the forex revenue for the country.

In view of the above, it is requested that the import duty for Industrial Ethanol be reduced to 0% in line (2.5% present duty) with duty on other competing feed stock to make ethanol based chemical.

(b) Reduction of Customs Duty on Feedstock Methyl Alcohol/Methanol (HS code: 29051100)

Methanol consumption in country is estimated at 1.8 - 2.0 million tones and is expected to reach 2.5 million tons by the end of the 12th five-year plan. The current production capacity in the country is 0.385 million tonnes/annum thereby creating a significant gap which would primarily be met through imports from Middle East and China.

On application side, the downstream products of methanol are Acetic Acid, Formaldehyde, Di Methyl Ether, Methyl Tertiary Butyl Ether, Gasoline etc. which are major basic building blocks for majority of chemicals in India. The removal in duty on methanol will surely boost the downstream industry and will reduce outgo of foreign exchange from country, also the resultant lower cost of production will increase the profitability of end products exported out of country. There exists strong opportunity in investment in methanol capacity in the country, but these are limited by feedstock (naphtha and natural gas) availability. In such a scenario, the government can incentivize the development downstream industry by removing custom duty on methanol. It is requested that basic customs duty on feedstock Methyl alcohol should be reduced to nil as this will promote growth of downstream chemical industry products.

(c) Reduction in customs duty on feedstock Acetic Acid (HS code: 29152100)

Acetic acid is an important organic chemical and critical building block/raw material for various downstream industrial chemicals like ethyl acetate, acetic anhydride, poly vinyl acetate etc. India is net exporter of these downstream products. India's total Demand of acetic acid is ~1 Million MTPA growing at 7.5% of which domestic production is ~15%, rest

~85% is import dependent. Further no domestic capacity is planned in next 5 years thereby increasing the demand supply gap unfavourably to Indian manufacturer. India is net exporter of acetic acid derivatives like Ethyl Acetate, acetic anhydride, PTA and other acetic acid derivatives. Acetic Acid is important feedstock for these products and to remain competitive in exports, a zero duty acetic acid imports are highly required. It is therefore requested that basic import duty on Acetic Acid should be reduced to Nil from the current level of 7.5%.

3.3.3. Inverted Duty Issues

(a) Ethyl Acetate (HS code: 29153100)

India is among the top 5 global producer and is a net exporter of ethyl acetate. India is dependent on Singapore for acetic acid imports. In view of the lopsided FTA, the company which supplies the acetic acid as well ethyl acetate has a cost and logistic advantage. India is not able to compete with them. Under the Singapore FTA, import of Ethyl acetate suffers 0% duty whereas Acetic acid which is used as input in manufacture of Ethyl Acetate is subject to 5% duty. Hence, there is an inverted duty structure which needs rectification.

It is suggested to revoke the duty rebate on ethyl acetate and exclude it from any ongoing/under-negotiation FTAs. Along with it the Government should provide duty free imports of Acetic Acid (HS code: 29152100) & Ethanol (HS code: 22072000). It is also requested that MEIS benefits should be given at 5% to make Ethyl acetate manufacturers competitive.

(b) Acetic Anhydride (HS code: 29152400)

India is net exporter of Acetic anhydride but net importer of the raw material acetic acid. The current capacity of the industry is sufficient to meet domestic demand. Under Singapore FTA imports of Acetic Anhydride is zero duty while its key feedstock is imported at duty of 5 to 7.5%. Though current imports are low but such duty structure is a probable threat for domestic industry.

It is suggested that Acetic Anhydride duty rebate be revoked and excluded from any ongoing/under-negotiation FTAs providing duty free imports of the feedstock Acetic Acid (HS code: 29152100). It is also requested that MEIS benefits should be given at 5% to make Acetic Anhydride manufacturers competitive.

3.3.4. Alkali Industry

Caustic soda, soda ash, chlorine are basic inorganic products that find applications in products of everyday use. Though India's share of global manufacturing capacity is very small, these are important segments that will grow, driven by mass consumptions and growing aspirations of our people. The "Make in India" programme of the government could provide the much needed impetus to make India self-sufficient in producing these products and reducing dependency on imports. The present global capacity of Caustic Soda is estimated at 94 million MTPA while India's capacity is only 3.66 million tonnes i.e. a mere 3.9% of the world capacity, while China has a capacity of 38.7 million tonnes i.e. almost 41% of the world capacity. Similarly the global Soda Ash capacity is 67 million MTPA. China has

the largest capacity at 32 million MTPA or 47.8% of total global capacity, while India's capacity is only 3.4 million tonnes i.e. 5%.

The Indian industry is facing challenges due to high power cost, cheaper imports and impact of cascading duties and taxes. These challenges affect the capacity utilization which is sub-optimal at about 82% for caustic soda and soda ash and about 95% for PVC. The following recommendations are made for consideration of the Government:-

(a) **Increase basic customs duty on imports of caustic soda and soda ash from 7.5% to 10%**

India is facing challenges due to cheap imports from low power cost countries in South, South East Asia & Middle East. Power tariff in India is among the highest in the world. In terms of technology, India is second only to Japan in adoption of latest technology by investing substantially. However, the high cost of power renders Indian manufacturing at a comparative disadvantage. Indian industry has adequate capacity to meet domestic demand for both caustic soda and soda ash. However, huge imports are affecting plant capacity utilization in the Indian industry. It is recommended that basic customs duty on imports of Sodium Hydroxide (Caustic Soda) (HSN 2815 11 and 2815 12) and on Disodium Carbonate (Soda Ash) (HSN 283620**)** be increased from 7.5% to 10%.

This will lead to higher plant capacity utilization and a level playing field for domestic manufacturers. Further, higher domestic production will reduce dependency on imports and save precious foreign exchange.

(b) **Provide full Exemption from customs duty on import of power equipment for captive power plants**

Caustic soda manufacturing is power intensive. Power constitutes 60% of cost of production. Erratic supply and non-availability of quality power has resulted in manufacturers setting up captive power plants at huge investment costs (per MW cost being about Rs.6 crores for coal-based power plants). Additionally state governments have imposed cess, electricity duty and various other taxes which add to the cost of power. The Caustic-chlor industry is power intensive. The industry has invested substantially in setting up captive power plants as grid power is insufficient to meet the exacting requirements of the industry. However, the duties and cess imposed by State government largely offset the advantages of setting up captive power plants. For a growing economy like ours, investment in infrastructure and power is essential to sustain the growth and add momentum to the "Make in India" campaign. Exempting customs duty on import of power plant equipment for captive power generation will improve the cost competitiveness of the Indian alkali industry and will result in benefits of higher employment. It is accordingly recommended that full exemption from customs duty on import of power equipment for captive power plants be provided and be reduced from the current 5% to Nil.

(c) **Duties/cesses on captive power generation to be subsumed in GST**

The industry has invested substantially in setting up captive power plants (CPPs) to meet its production needs. However, State governments have been imposing electricity duties and cesses on captive power generation which has the effect of largely negating the advantage

in setting up CPPs. Subsuming electricity duty and cess in GST will improve the competitiveness of the industry. The reduction in revenue will be largely offset by higher revenue due to higher competitiveness, increased production/output.

3.3.5. Chemical Clusters

The Chemical Industry has special requirements of dealing with toxic effluent discharge. The provision of common facilities in the form of good quality power/water supply, effluent treatment/incineration, testing and other logistic facilities such as chemical storage tanks, telecom/firefighting and rail/road connectivity/boilers etc. can facilitate the sector. Further, if related industries are set up in close proximity in an industrial estate, they could be vertically integrated resulting in a saving on the transfer cost of feedstock and finished goods. This, coupled with lower investment on infrastructure as a result of sharing, would tremendously improve their cost competitiveness. This will also help in containing the environmental load linked to the chemical industry. Such clusters could also be the points where migrating industry from west lands. Existing hubs (brown field) will need slightly different approach. Department of Chemicals and Petrochemicals is already facilitating cluster approach in plastics sector. A similar approach is required for the chemical sector.

3.3.6. Technology up-gradation Fund for Chemicals Industry

To remain globally competitive and comply with requirements of international conventions, Indian chemical industry needs to upgrade its technology to meet world standards and show improved performance in global trade. The industry, especially the micro, small and medium enterprise sector, does not have access to capital to upgrade technology on its own. Also, non-availability of technology leads to imports in some technology-intensive sub-segments. To address these issues, the government may establish a "Technology Up-gradation & Innovation Fund" (TUIF) that can address specific technology issues, faced by the industry. The fund should also support setting up of common chemicals infrastructure (e.g. effluent treatment plants, chemical waste disposal plants, etc.), which would benefit industries and the environment. From this fund support may be extended to the chemical industry for technology up-gradation at lower rate of interest. This will help industry in improving quality of output and become more competitive. The same can be similar to Technology Upgradation Funding scheme in the Textile sector.

3.3.7. Petrochemicals

The petrochemical industry being an "enabler" to all other sectors of the economy, has the potential to emerge as one of the prime drivers for industrial as well as economic growth. For this a facilitative policy regime is required which can be provided by addressing key fiscal issues that are currently being faced by this sector. Growth in the petrochemical industry facilitates the development of the downstream industry which creates large-scale employment and hence, can go a long way in addressing the national challenge of generating additional employment in the country.

The domestic petrochemical industry has made huge investments in creating capacities for products like Polyethylene and Polypropylene including new capacities commissioned this

year. In order to maintain the financial viability of these new investments, adequate fiscal support is critical. In certain key products like Poly Vinyl Chloride, investment has been severely lagging demand growth due to a lack of a facilitative fiscal structure. This is undermining the "Make in India" campaign and the vision for making India a manufacturing hub. On account of the inadequate domestic capacity for products like PVC, large volume imports continue to take place resulting in huge foreign exchange outflow. If the situation is not addressed, it will continue to worsen contributing towards widening the country's trade deficit.

In the above back-drop, FICCI would like to make the following submissions for the Government's consideration:-

1. Import duty on polymers like Polyethylene, Polypropylene, Poly Vinyl Chloride and Polystyrene in India are way below the same in peer countries as is the duty differential between polymers and feedstock naphtha. India already had substantial surplus of Polypropylene and has added massive new Polyethylene capacities this year which has created huge surplus for Polyethylene as well. For Poly Vinyl Chloride, no new capacity has been added in the country for over a decade despite demand exceeding existing capacity consistently. In view of the surplus in Polyethylene and Polypropylene and the need for a facilitative fiscal structure for the development of the domestic PVC industry, import duty on polymers like Polyethylene, Polypropylene, Poly Vinyl Chloride and Polystyrene, be increased from the existing level of 7.5% to 10%.
2. Polyethylene Terephthalate (PET) is a petrochemical product derived through polymerization like other plastic raw-materials in chapter 39. However, while most of the major plastic raw-materials attract 7.5% duty, the same on PET continues to be 5%. PET is a vital raw material used both by textile and the packaging industry. With the exponential growth of the retail sector in India, demand for packaging and consequently, demand for PET is expected to soar. India already has augmented large domestic PET capacity involving substantial investments and the country is a net exporter. It is proposed that import duty on PET (HS code: 39076100) may be raised from the existing level of 5% to match the duty on other major commodity polymers as listed in point no. 1 above (at least 7.5% or 10%, if duty on other polymers is raised to 10% as proposed).
3. ABS and SAN are engineering plastics - advanced materials with superior properties used in critical applications in automotive, appliances, electrical and electronic sectors. The domestic petrochemical industry has made sizeable investments over the years in creating ABS and SAN capacity in the country for meeting requirements in these critical applications. It is recommended that import duty on ABS (HS code: 39033000) and SAN (HS code: 39032000) be increased from 7.5% to 10% aligning this with other major plastic raw-materials.
4. India has a huge textile industry comprising of natural and man-made (synthetic) fibres. Polyester is the key pillar of India's robust synthetic fibre industry. PTA and MEG are two key fibre intermediates which go into polyester production. Indian MEG industry has potential for sustained growth, on the strength of growth in the Indian Polyester

Industry, which is the World's 2nd largest after China. In response to this growth potential, Indian companies have invested/ are investing in new MEG plants, with substantial capital expenditure. In fact, in the current year itself a million ton of new MEG capacity has been added in India. Indian MEG industry faces threat from very low cost producers in the Middle East, and upcoming capacities in the US, who all have access to very cheap Gas feedstock. Power cost, which is the major component of the conversion cost for MEG, is higher in India than these countries. So are automotive fuel prices and hence transport costs. India has the lowest custom duty on MEG, amongst the major MEG consuming countries. A higher degree of duty protection will promote continued domestic investments, provide raw material for the Polyester industry, contribute to GDP & tax revenue growth.

5. Butadiene is the key input for synthetic rubber and currently attracts 2.5% duty. The synthetic rubber sector in India is already under tremendous pressure on account of the FTAs in operation and low margins. To provide some support to the synthetic rubber industry, it is proposed that import duty on Butadiene (HS code: 29012400) is reduced from the existing 2.5% to nil. Also, duty on crude Butadiene (HS code: 27111900), feedstock for Butadiene, be reduced from existing 5% to nil**.**

6. Feedstock cost accounts for a major part of cost of production in petrochemicals. In Budget 2014-15, duty on most key petrochemical feed-stocks was reduced to 2.5% with the exception of Naphtha. Naphtha is one of the most widely used feed-stocks in India with over 50% of India's cracking capacity being Naphtha-based. Naphtha is also used for power and fertilizer production, wherein for fertilizer production it is exempt from import duty. Import duty on Naphtha in India at 5% is one of the highest, and consequently, the duty spread between the feedstock and end-product polymers in India is one of the lowest globally. In most countries, import duty on Naphtha is nil as it is the basic input for the industry.

   Import duty on key petrochemical feedstock Naphtha (HS code: 27101290) may therefore be reduced to Zero. This in turn would increase the duty spread between the feedstock and end-product (polymers) and incentivize domestic manufacturing.

7. Mixed Petroleum Gas is another basic "feedstock" for the chemical and petrochemical industry. In order to enhance the cost competitiveness of the industry, import duty on Mixed Petroleum Gases (HS code: 27112900) also be brought down from 5% to 2.5%.

8. EDC and VCM are key raw materials for production of PVC, a key polymer. Styrene is the principal raw material for Polystyrene. There is very little production of EDC and VCM for merchant sale within the country and the existing domestic capacity is essentially for captive use. Hence PVC producers have to meet their requirements through imports. Similarly, there is no domestic production of Styrene and the entire Styrene requirement of the country is imported. Both PVC and Polystyrene margins are under severe pressure and manufacturers are facing significant hardship. To provide relief to both these products through reduction in input cost, import tariff on key petrochemical inputs EDC (HS code: 29031500), VCM (HS code: 29032100) and Styrene (HS code: 29025000) may be brought down from the existing 2% to zero.

9. Import duty on Palladium Catalyst continues to be high at 7.5% compared to the catalysts used in other industries. Palladium catalyst requirement in the country is essentially met through imports. Import duty on Palladium Catalyst (HS Code: 38151210) be reduced from the existing 7.5% to 5% to bring it at par with catalysts used in other industries and to provide some relief to user industries.

3.3.8. PVC INDUSTRY

Poly Vinyl Chloride (PVC) is probably the most important plastic. It is a basic product that goes into serving the basic needs of Indian people. Today unfortunately more than 1.7 million tons of PVC, representing almost 60% of the local demand, is imported into the country due to lack of local investment. The lack of incentive for creating local capacity in India has meant that, while PVC demand in India is growing at a rapid rate, unfortunately it is being serviced by imports. This is also starkly brought out by the alarming increase in imports on a YoY basis – in the decade between FY 2006-07 and FY 2016-17, while overall demand grew by a CAGR of 9%, imports have grown from 300kt to 1,590kt, a CAGR of 18%. It is requested that some fiscal measures as detailed below be considered. This would apart from having a positive impact on the exchequer, would give a big fillip for growth and investment in the PVC sector in India.

3.3.9. Technology Upgradation Scheme for the Plastics Industry

- Existing units need upgradation/installation of new plant and machinery in place of old plant and machinery. Technology upgradation fund scheme (TUFS) for Plastics industry is needed. This will provide loan to units at subsidized rates to Plastics Processors for the purchase of new machinery for upgradation.
- Significant technology advancements in Plastics Machinery have taken place in recent years. Technologies to improve productivity were available since 2000; technologies to improve energy efficiency were available since 2007 -2009 period. The Indian plastics processing and converting industry has large population of older technology machinery and thus does not have the same technological edge to remain competitive in costs and quality compared to our global competitors. This is mainly in the plastics moulding, extrusion and flexible packaging converting industry. To gain competitive edge, processors need to replace the older machinery with new modern technology machines.
- Proposed scheme is the scheme for modernisation and technology upgradation in the plastics processing and converting sector.
- The proposed scheme aims at making available funds to the domestic plastics processing and converting industry for technology upgradation of existing units as well as to set up new units with state-of-the-art technology so that its viability and competitiveness in the domestic as well as international markets may enhance.
- There is increasing competition from China and other countries not only in the international market, but also in the domestic market. To meet the challenges the industry is required to become competitive, cost effective and quality oriented. Though

industry is gearing itself for this challenge, but simultaneous help and assistance is required from Government of India particularly for modernization of industry.

CIGARETTES

3.4.1. Rationalise rates of GST/GST Compensation Cess on Cigarettes

The incessant increase in cigarette taxes over the past several years has taken its toll by way of substantial fall in the volume of duty-paid cigarettes. Since 2011-12 the increase in rate of tax on cigarettes is a staggering 202% – far ahead of the growth of per capita GDP (63%) and inflation (CPI – 45%) over the same period.

The upward revision of the advalorem component of GST Compensation Cess from 5% to 36% on King Size Filter Segment (KSFT) has resulted in a 19% (weighted average) increase in tax for this segment. Since the bulk of the smuggled international brands of cigarettes are in the KSFT segment, the sharp increase in duty for this segment has only served to make the tax arbitrage, and hence, illicit trade more attractive. The high tax cost of duty-paid cigarettes drives consumption of tobacco to other, revenue inefficient tobacco products like biris, chewing tobacco, khaini, guthka, etc. Simultaneously, the price increases that the legal industry was compelled to undertake in the wake of the tax increase under GST has resulted in vacation of critical price points at the value end of the market. The consequent vacuum has been rapidly filled up by domestic illicit cigarettes at stick prices that are even below just the tax cost of a duty-paid cigarette.

Due to punitive and discriminatory taxation, duty-paid cigarettes contribute more than 87% of tobacco revenue whilst accounting for merely 11% of total tobacco consumed in the country. This issue has been addressed partly in the GST regime with all tobacco products taxed at a uniform rate of 28%. Whilst this is a very welcome step, the wide disparity of tax between cigarettes and other tobacco products continues. For example, machine made biris are subjected to GST @ 28% and a specific tax of Rs. 2/- per M in comparison, the tax applicable on Micro Filter cigarettes (the segment closest to Biris in terms of length) is GST @ 28%, GST Compensation Cess @ 5% (advalorem) and specific tax (comprising NCCD and GST Compensation Cess) amounting to Rs. 2,166/- per M. This disparity needs to be addressed urgently.

For cigarettes a balanced, practical and non-discriminatory taxation policy combined with strict measures for curbing illicit trade and tax evasion are required for resolving the crisis of tobacco farmers and mitigate the immense hardship of the legal cigarette industry, within the overall tobacco control objectives. It is suggested that rationalisation of rates of GST / GST Compensation Cess on cigarettes across all segments be considered. It is further suggested that increase in the rate of advalorem GST Compensation Cess to 36% for King-Size cigarettes (>75mm in length) to 5%, in line with the levy of 5% advalorem GST Compensation Cess on all the other length segments be considered. This measure will help combat the contraband trade in international brands of cigarettes smuggled in to the country, the bulk of which belong to the King-Size segment.

3.4.2. Allow Input Tax Credit of Additional Duty Surcharge embedded in Transition Stocks

In terms of the transitional provisions of the GST laws the Additional Duty (Surcharge) or, ADS has been excluded from the list of eligible taxes embedded in transition stocks for which input tax credit is available. This, notwithstanding the fact that input tax credit of ADS was permissible under the Cenvat Credit Rules, 2004. The denial of input tax credit for this has resulted in an inequitable situation, whereby effectively, ADS has been levied on transition stocks although, in the GST regime no such tax is applicable on cigarettes, and there has been significant cascading of GST and advalorem GST Compensation Cess on the ADS component embedded in the transition stocks.

The steep increase in cigarette taxes under the GST regime compelled increases in prices of duty-paid cigarettes. Consequently, critical price points have been vacated by the legal industry and the resultant vacuum has been filled in rapidly by illicit, tax evaded cigarettes – both domestic as well as international. The growing onslaught of contraband trade has created additional pressure and hardship for the legal cigarette industry. It is suggested that some relief is provided to the legal industry and the trade by permitting input tax credit of ADS embedded in transition stocks of cigarettes.

CIVIL AVIATION

3.5.1. Zero Rating for Maintenance, Repairs and Overhaul Industry

Maintenance Repair and Overhaul (MRO) industry is engaged in the business of providing engineering support to the local airline companies by undertaking repair and maintenance of aircraft and related components. The prevailing archaic rules continue to allow import of such aviation MRO services from foreign based MROs on duty/tax free basis, whilst Indian MRO companies are required to conform to the tax/duty regime, thereby increasing the cost of same services by Indian MRO companies by 20% to 25%. This has resulted in shutting down of 30% of units in India over the last few years. Due to the adverse tax regime, no investment has taken place in the last few years in this sector. It is accordingly recommended that zero rating be prescribed for the Indian aviation MRO industry under the GST regime.

EDUCATION

3.6.1. Higher Education

A. To address the shortage of faculty in the country, the Government should expedite the launch of National Mission for Faculty Development and provide a tax relief to the tune of 50% to Universities/Higher Educational Institutions that spend on the capacity development and training of their staff.

B. Given the priority of Skill Development in the national agenda , Government should make the following provision;

   - Any person enrolling for a Skills Certification course be eligible for a 20% tax rebate (only applicable for the tuition fee amount)

- Any Educational Service Provider opening a Skills Centre in a backward area should be given an exemption from income tax for the first 3 years.

C. To augment investment in the higher education sector, all donations (and not just restricted only to research funding) to qualified Higher Educational Institutions should be eligible for 200% tax deduction.

D. New or existing educational institutions making a fresh investment of Rs. 75 crores or above should be eligible for a preferred and long term Loan facility with interest rates at par with Base Rates or Prime Lending Rates of the commercial banks or financial institutions and for a tenure of up to 15 years with step up repayment plan.

E. Higher Educational Institutions should be free to set up campuses overseas freely and a line of credit of at least $500m should be set up by the Exim Bank, as a part of India's diplomatic efforts and use of soft power.

F. As per the Notification No. 12/2017 – Central tax (rate) the input services received by education institutions which provide education beyond higher secondary school are a taxable supply and GST is applicable. Therefore, GST is payable inter-alia on the following services:-

- Software required for educational purposes or for maintaining database of students;
- Services in relation to examination e.g. Rent payable to Examination Centers, professional Charges payable to Agency hired for conducting of examination;
- Security Services, Housekeeping Services, Transportation Services for students, staff & faculty, IT Expenses, Purchase of Software/Licenses;
- Mess Charges;
- Professional Fees payable to various consultants;
- Advertisement.

Self-Financed Institutes procure research equipments which were earlier exempted from excise duty (referred to as 'DSIR exemption') but the same has not been continued in GST regime. The rationale for such withdrawal of exemption under GST regime is that credit is available if tax has been paid. This is not fully applicable to institutions which are providing predominantly exempted educational service for which credits cannot be used. It is recommended that the exemption available earlier in excise should be extended in GST regime for research institutions in respect of such goods.

All the above factors will result in an increase in the cost of education. With the additional impact of GST, privately funded educational institutions will be constrained to pass on this additional cost to students. It will also adversely affect the resolve of the Ministry of Human Resource Development to increase the Gross Enrolment Ratio (GER) in Higher Education from the present 23.6% to 30% by the year 2020. It is requested to provide exemption to privately funded educational institutions from payment of GST on all the input services on which no service Tax was payable even under the erstwhile tax regime.

3.6.2. School Education

A. Use central funds strategically to spur policy reform in states

The Centre can create a Rs. 1000 crore 'State Policy Reform Fund' to incentivise states that implement measures such as merit-based headmaster selection, transparent process for teacher recruitment, allotment and transfers and merit-based teacher promotions.

Central schemes such as Jawaharlal Nehru National Urban Renewal Mission (JnNURM) have successfully used a similar approach for influencing states' policies. Under JnNURM, 75% of the grant was subject to achievement of policy reforms.

B. Education quality and capacity building of existing institutions

The country needs setting up of new specialized research and training institutes with focus on areas such as standardized assessments, school leadership, early literacy & numeracy, pedagogy etc. These should be set up as autonomous bodies such as the National Skill Development Corporation and a corpus of Rs. 200 crore can be allocated for this purpose.

Additionally, there is a need to adequately resource and build technical capacities of existing central institutions such as NCERT, NUEPA, IGNOU, CIET and NIOS.

C. Strategic initiatives such as assessments, ICT and teacher/headmaster development

There is a need to substantially increase investment on student learning assessment surveys from the current Rs. 12 crore to Rs. 100 crore so that states have sufficient funds for instrument development and implementation, dissemination of results across stakeholders and training of functionaries in the use of assessment data for designing quality improvement interventions. It is recommended that a 50 per cent increase in the spending on the teacher education scheme as this is critical for strengthening teacher education institutes across states.

D. The tax structure for schools under pre-GST regime was more facilitating than under GST due to the following reasons:-

- The aggregate turnover for the determination of registration requirement under Service tax specifically excluded exempt supplies, which is in contradiction of the definition of aggregate turnover under GST;
- The threshold limit for state VAT was calculated for each state separately and the turnover of output services was not counted for the purpose of calculating threshold for VAT purpose. This kept schools/organisations with exempted supplies out of the threshold limit for their non-business activities like sale of used furniture etc.

While law intends to keep the suppliers of exempted goods/services free from GST registration, however, the liability for schools to register under GST and undertake all the compliances is clearly against the intention of the law makers. To mitigate the negative impact on schools, the following recommendations are made:-

a) Exempted supplies should not be included for calculating threshold limit

It should be provided that since schools are engaged in the 'business of supplying exempted 'supplies', the transactions like sale of used assets which does not even constitute as a

regular 'business activity' should not require schools to obtain GST registration and undertake monthly compliances. Or Alternatively, it should be specified that the schools which are engaged in provision of 'exempted services', should not be required to obtain GST registration in case the taxable transactions from 'non-business' activities does not exceed 7.5% of the total turnover. This would not entail any revenue loss to the Government since the applicable GST is already paid on the procurements by school which is not even claimed as input tax credit.

b). Reverse charge should not apply to Schools providing exempted education service

As the GST law require recipient to obtain registration in case of any specified procurements, schools should be provided specific exemption from GST payable under reverse charge. It should be specifically provided that "Services received by Primary, Secondary or Higher Secondary schools providing education services which are exempt from GST are exempt from payment of tax on procurements under reverse charge''.

FINANCIAL SERVICES

I – INSURANCE

Direct Tax

3.7.1. Adjustment of TDS in case of Free Look Cancellations

Insurance Regulatory and Development Authority (IRDA) allows policyholders to cancel the policy during the free look period (currently set to 15 days). In case of cancellations during free look period, the commission income accrued/paid to agents needs to be reversed/ recovered. It should be provided that taxes that were already deducted under section 194D of the Act and paid to the Government Treasury on the commission amounts, which no longer would be payable on account of free look cancellations, should be allowed to be adjusted in meeting the subsequent TDS liability of the insurers or alternatively, a mechanism should be laid down for claiming refund of such excess TDS deposited. A plain reading of section 194D of the Act suggests that TDS has to be deducted on the entire amount credited to the agent's account and not to the net amount (i.e. agent's commission adjusted with subsequent debits such as for free look/ cancellation of any policy). CBDT Circular No.120 dated 8 October 1973 clarifies that TDS has to be effected on the gross credit/payment and adjustment is not permissible. In such cases, it is a loss of funds to the insurer if the same is not allowed to be adjusted in the subsequent Tax Deducted at Source (TDS) payments of Insurer or he is not allowed to claim the same as refund. It is suggested that suitable amendment in section 194D of the Act be made to provide that the amount of TDS if any should be allowed to be adjusted against the future payouts to agents, on account of cancellation of policy during its free look period.

3.7.2. Period of Carry Forward and Set-off of Losses in Case of Insurance Business

The insurance industry has a long gestation period and it takes a long time to achieve a break-even. Accordingly, the limit of 8 years for carry forward and set off of business losses is not sufficient. Considering the importance of Insurance Sector for the Indian economy, it

should be allowed to carry forward and set-off unabsorbed business losses for an indefinite period.

3.7.3. Enhanced Deduction of Life Insurance Premium under Section 80C of the Act

Section 80C of the Act basically provides for a deduction up to Rs. 150,000 for investments made in various savings instruments such as mutual funds, bank deposits along with long term savings in life insurance plans, pension plans, etc. Various other expenditures like tuition fees etc. have also been included. Due to such inclusion, share of investment for allowable deduction is reduced to large extent. In order to encourage growth in the life insurance segment it is recommended that the Government should increase the limit of deduction for life insurance premium/by creating a separate limit for deductibility of life insurance premium to the extent of Rs. 200,000 along with an overall enhancement in the investment limit under section 80C of the Act to at least Rs. 300,000.

3.7.4. Applicability of MAT on General insurance companies

Like Life Insurance companies even for General Insurance companies, the provisions of MAT under section 115JB of the Act should not apply. To provide parity with Life Insurance companies even the General Insurance companies should be exempted from the levy of MAT under section 115JB of Act.

3.7.5. Applicability of exemption under section 10(34) and 10(38) to insurance companies

There is ambiguity around applicability of exemption under section 10(34) and section 10(38) of the Act to insurance companies. It is suggested that appropriate clarification should be issued explicitly stating that exemption under section 10(34) and section 10(38) of the Act is applicable to the insurance companies.

3.7.6. Profits from Life Insurance Business

Rule 2 of First Schedule of the Act pertains to the computation of profits of life insurance business wherein the annual average of the surplus arrived in the inter-valuation period is taken as profit of the insurance business disclosed by the actuarial valuation made in accordance with the Insurance Act, 1938 (4 of 1938). The new format of Form I under the Insurance Regulatory and Development Authority (IRDA) Act requires maintaining shareholders' account and policy holders' account separately which could imply that shareholders' account does not form part of life insurance business.

A clarification should be issued wherein it should be clarified that the total of Policyholders account and Shareholder account should be taken as profits from life insurance business. Accordingly, shareholder's account and policyholder's account be considered as part of one single business and tax be levied at the rate of 12.50% under the provisions of section 115B of the Act.

3.7.7. Taxability of Re-insurance Premiums earned by Foreign Re-insurers

An Indian insurance company can avail re-insurance with either an Indian re-insurance company or a foreign re-insurance company. The Act does not contain specific provisions for taxability of foreign re-insurance companies. CBDT has issued Circular No. 35 of 1956

dated 3 September 1956 in respect of taxability of a foreign company engaged in re-insurance with Indian companies. The aforesaid circular states that no uniform principle could be laid down which will be applicable in all cases and that the taxability would need to be determined based on facts and circumstances of each case. The re-insurance premiums earned by foreign re-insurers from Indian insurance companies are in respect of re-insurance agreements which are concluded outside India. Further, the source of income for the re-insurers is their financial assets and risk taking capacities which are entirely located outside India.

However, the tax authorities have in some cases, adopted a contrary view and concluded that the presence and activities of group entities in India rendering services to the foreign re-insurer constitute a PE for the foreign re-insurer in India. Moreover, in the recent past, the tax authorities have in the case of some foreign re-insurers initially taken a view that ceding re-insurance premium is taxable in India as the ceding Indian insurance companies constitute a dependent agent PE of the foreign re-insurer in India. Accordingly, payments made by Indian insurance companies to foreign re-insurers are disallowed due to reason of non-withholding of taxes.

In addition to the above, the Insurance Regulatory and Development Authority of India (IRDAI) has also issued a separate set of Regulation permitting foreign reinsurers to set-up branch offices in India to carry out re-insurance business. However, the provisions of the Act per se do not provide for the mechanism in which foreign reinsurers are required to offer their income to tax in India.

In order to allay the apprehension of foreign re-insurers, it is recommended that a separate taxation regime should be introduced, keeping in mind the peculiarities of the reinsurance business. The following recommendations are made in this regard:-

- For reinsurance companies without branches, since no profits accrue or arise in India, reinsurance companies not having a branch in India should not be taxed in India and consequently no tax should be withheld from the reinsurance premium paid to such companies.
- For reinsurance companies/branches in India, the tax rate can be initially fixed at 25% for the Indian policies. This rate can be gradually reduced in a phased manner so as to be competitive with global tax rates. In addition, we suggest a tax rate of 10% for the non-Indian (global) policies to help India become an international reinsurance centre.
- When the reinsurance premium is paid, it is a 'gross receipt' and not a 'profit 'for reinsurers, as they underwrite some of the risks of the insurer and would have to honour the claims arising thereafter. As the Indian branches of foreign reinsurers would operate on "thinner margins", withholding tax at 43.26% on "gross amounts" (receipts) would not only pose a serious cash flow issue for such branches but also would lead to a significant administrative burden of following up for refund of excess withholding tax. Further, this would make business unviable for such branches, with implications for the entire Indian insurance industry and also defeating the purpose of Insurance Act (Amendments) 2015 that allowed reinsurance branches to be set up in India. Currently,

Indian branches of foreign banks are allowed to apply for and obtain a NIL withholding tax certificate from the tax authorities, thereby enabling these branches to receive interest and other sums without deduction of withholding tax. The Indian branches of foreign reinsurers be allowed to apply to the tax authorities to obtain a NIL withholding tax certificate. Alternatively, foreign reinsurers should be allowed to discharge their tax liability by way of advance tax mechanism.

- MAT should not be made applicable to such a highly regulated industry, in line with Life insurance business.

GST

3.7.8. Provide for no ITC reversal due to transaction in securities

The Insurance Regulatory Development Authority ('IRDA') mandates Life Insurance Companies to invest in specified securities. The mode and extent of the investments are determined in terms of the guidelines issued by IRDA (Refer Notification No. F. No. IRDAI/Reg/22/134/2016 dated 1 August 2016). Investment in securities as mandated by the Regulator are held for meeting the obligations to the Policyholders. The Life Insurance Companies are not permitted to use or access the monies invested in accordance with the IRDA guidelines. Transaction in securities is part of life insurance business and not as an investment function. Life Insurance companies are also not permitted to undertake any other business other than Life Insurance business. Securities are excluded from the definition of goods as well as services as per the provisions of GST laws and hence transaction in securities shall not be liable to GST. However, as per provisions of section 17(3) of CGST Act, the value of exempted supply shall include transactions in securities. It needs to be clarified as to whether the pooling of funds and investments in specified securities by the Life Insurance Companies be treated as 'transactions in securities' having impact of the claim of Input Tax Credits by the Life Insurance Companies.

It is further recommended that considering the mandatory requirements laid down in terms of the IRDA Regulations, 2016, investment in securities should not be treated as 'transactions in securities' and accordingly exempt supply for the purpose of calculation of reversal of ITC.

3.7.9. Provide clarity on location of the Supplier of Services in case of Fund Management Charges

In the case of Unit Linked Insurance Policies ('ULIP policies'), the Life Insurance Companies recover a Fund Management Charge ("FMC") towards managing and administering the fund for the policyholders. The FMC is levied on the Assets under Management ("AUM") and is charged on a daily basis and recovered from the Fund as a whole and is not attributed to a single policy. As a result of the levy of FMC, the Net Asset Value ("NAV") of the ULIP units held by the policy holder would reduce. The funds are managed centrally by the Fund Management team, which is located at a single location in India. Considering that the funds are managed by the Fund Management team and proposals/policies are sourced on PAN-India basis, the question arises about the 'location of the supplier of services' in the case of the FMC levied and recovered. It is believed that as per section 2(15) of the IGST Act, 2017,

the 'location of the supplier of services' in such a case should be the location where the fund management team is situated. Accordingly, the above charges would be reported at a State level i.e. on the basis of the address of the policyholders in the return in GSTR-1. It is requested that appropriate clarity in this regard may be duly provided.

3.7.10. Corporate Agents to be under Forward Charge

As per Notification No 13/2017 – Central Tax (Rate) dated June 28, 2017, life Insurance Companies are required to pay tax under reverse charge mechanism for commission paid to insurance agents. Life Insurance companies compute and pay the commission amount to its agents periodically. Life Insurance agents are either Individual Agents (unregistered) or Corporate Agents (registered). The GST Law mandates every registered person to raise a tax invoice for the supply of service [Section 31(2) of the CGST Act, 2017].

In light of the above, registered corporate agents will raise an invoice for the policies sourced by them. It is envisaged by the Life Insurance companies that the following challenges may arise with respect to payment of commission to corporate agents:-

a) Payment made to the corporate agent basis the policies sourced by the agent but invoice not raised and uploaded in GST Network by the corporate agent;

b) Tax is paid by the Company based on the commission computation and payment to the corporate agent, however invoice may be reported in the subsequent month by the corporate Agent.

c) Challenges in reconciliation of mismatch reports, as there is possibility that tax liability discharged by the insurer may be different from the amount reported by the corporate agent.

It is emphasized that since corporate agents will be required to be registered under the GST Law, hence payment of commission to registered corporate agents should be made liable to tax under forward charge mechanism. It is accordingly suggested that appropriate amendment be made to the aforesaid notification to include only supply of services from "insurance agent being an individual" under reverse charge mechanism.

3.7.11. Treat Policies issued to Non-resident persons as Export of Services

Life Insurance policies are issued to Non-Resident Indians (NRIs). Under the guidelines issued by the Regulator i.e. IRDA, the premium collected is required to be received in Indian Rupees only, that is, the foreign currency exchange risk should not be borne by the Life Insurance Company. Accordingly, in many cases, the premium towards the insurance policies issued to NRIs is received from the Non-Resident External ('NRE') accounts held by the insured. The amounts held in this account are classified by the Reserve Bank of India equivalent to foreign exchange and can be utilized to payment towards export of goods or services (Refer RBI/2016-17/93 / A.P. (DIR Series) Circular No. 11 [(1)/14(R)] October 20, 2016). It is not clear as to whether the insurance premium received from the NRE accounts of the policyholder satisfy the condition of receipt of consideration in 'convertible foreign exchange' and therefore, constitute 'export of services' for the purpose of section 16 of the IGST Act, 2017. If considered as export, whether life insurance companies would be required

to comply with requirements for submitting a Bond/Letter of undertaking, in cases where the company exports without payment of IGST, in terms of section 16 of IGST Act read with Rule 96A of CGST Rules.

It is submitted that NRE accounts are opened and held by Non-Resident Indians from convertible foreign exchange and the amount held in this account can be freely repatriated by the accountholder. It is therefore suggested that the premiums received from NRE accounts should be treated as receipt in convertible foreign exchange and, therefore, meeting the requirements for export of services. It is further submitted that the life insurance companies should not be required to comply with the requirement to submit a LUT for export of services (policies issued to NRIs).

II - NON BANKING FINANCIAL COMPANIES (NBFCs)

Direct Tax

3.7.12. Treatment of Recognition of Income

Section 43D of the Act recognizes the principle of taxing income on sticky advances only in the year in which they are received. This benefit is already available to Banks, Financial Institutions, a co-operative bank (other than a primary agricultural credit society or a primary cooperative agricultural and rural development bank) and State Financial Corporations. In accordance with the directions issued by the RBI, NBFCs follow prudential norms and like the above institutions are mandatorily required to defer income in respect of their non-performing accounts. Various judicial precedents have held that interest income on NPA's under the provisions of the Act should be chargeable to tax only on receipt basis following the principle of real income.

Further, the Central Board of Direct Tax ('CBDT') has recently notified the Income Computation and Disclosure Standards ('ICDS') which are effective from AY 2017-18. As per ICDS IV on Revenue Recognition, interest income shall be recognised on time proportionate basis i.e. on accrual basis.

This has been further clarified by the CBDT in its recent FAQs issued on 23 March 2017, which provides clarification on various aspects of applicability of ICDS. As per Question 13 of the FAQ, it has been clarified that interest accrues on time basis. Further, as per Question 2 of the FAQ, CBDT has also clarified that provisions of ICDS shall prevail over past judicial precedents (thus overriding the real income principle laid down by various judicial precedents).

In view of the above CBDT clarifications, it may be challenging for NBFCs (other than housing finance companies) to adopt the position of taxing interest on NPA on receipt basis, severely impacting their cash flows and liquidity.

Considering the fact that similar to Banks, NBFCs are also engaged in financial lending to different sectors of the society, the Finance Act 2016, has expanded the scope of section 36(1)(viia) of the Act, by providing deduction to the extent of 5% of total income in respect of provision for bad and doubtful debts to NBFCs.

However, in absence of specific coverage of NBFCs (other than housing finance companies which are already covered by the provisions of section 43D) in section 43D and in light of the ICDS provisions, NBFCs would be required to recognise income on such NPAs for tax purposes on an accrual basis, resulting in levy of tax on income which may not be realised at all. This would severely impact the liquidity of NBFCs in terms of cash flow pay-outs, impacts their profitability and also has a consequent impact on their cost of operations.

In light of the above, an amendment should be made to section 43D of the Act, to extend the benefit of section 43D to "Non- Banking Financial Company" (other than housing finance companies which are already covered by the provisions of section 43D), whereby interest income on non-performing assets should be taxed only on receipt basis. Accordingly, consequential amendment should also be made in Rule 6EA of the Income Tax Rules, 1962 ('the Rules') which provides special provision regarding interest on bad and doubtful debts of banks and financial institutions, to include the "Non- Banking Financial Company" as well. NBFCs are an indispensable engine to fuel the economic growth and benefit under section 43D of the Act can help NBFCs in reducing their overall cost and consequently their lending rates.

3.7.13. Exclusion of interest/processing charges paid to NBFC from the provisions of Section 194A of the Act

As per section 194A TDS @ 10% is required to be deducted on interest payment including processing charges under loan/finance arrangement, however, banking companies, LIC and Public finance institution are exempt from purview of this section. NBFC carry on loan/finance business to mostly retail customers who are in organized sectors which includes large number of individual, Partnership firms and SMEs. This provision puts NBFCs in a disadvantage position and creates severe cash flow constraints since NBFCs operate on a very thin spread /margin interest. Margins are very low compared to TDS on interest and processing charges. Further, NBFCs have to face severe hardship in terms of collection of TDS certificates from their customers whose numbers run in thousands. Therefore, payment of interest to NBFCs (including those which have been accorded Public Financial Institution status) should be excluded from the purview of provisions of Section 194A of the Act. This will provide level playing field to NBFCs similar to banking companies, LIC, UTI, public financial institution etc., which are also exempted from the purview of this Section.

3.7.14. Higher depreciation rate on Plant & Machinery given on lease by NBFCs

Depreciation rate on General Plant & Machinery is at present 15% in all cases including for the NBFC companies which are engaged in the business of leasing of assets. NBFC companies has no control on normal wear and tear of the assets and no control on its use.

In view of the rapid obsolescence and user of the assets are different than the NBFC companies, the assessee has no control over the use of the assets and the lowered depreciation is not adequate to meet the requirement of replacement of the asset or depreciation in value of low value assets. It is suggested that depreciation on such Plant & Machinery should be allowed at higher rate.

3.7.15. Exclusion from applicability of provisions of section 269T

The Finance Act 2017 introduced section 269ST in the Act, which prohibits receipt of cash exceeding Rs. 2 lacs with a view to curb the black money and promote digital economy. It provides that no person shall receive an amount of Rs. 2 lakhs or more in aggregate from a person in a day or in respect of a single transaction or in respect of transactions relating to one event or occasion from a person otherwise than by an account payee cheque or an account payee bank draft or use of electronic clearing system through a bank account. Banking companies, post office savings bank, co-operative banks have been excluded from the applicability of this section. As per the current provisions, the section applies to NBFCs as well. Applicability of this section to NBFC companies will adversely impact the overdue collections from customers – Given the nature of business of NBFC, there are huge number of defaulters and the companies are required to make tremendous efforts to recover outstanding dues. By restricting the mode of recovery as above, this may have huge impact on the recoveries and consequentially lead to increase in bad debts.

Considering the business model of NBFCs and huge adverse impact on the recoveries and consequentially leading to increase in bad debts, NBFCs should be excluded from the applicability of this section.

3.7.16. Interest deduction limitation under section 94B

Provisions of limitation in deduction of interest are not applicable for banking and insurance companies, the same needs to be extended to NBFCs as well. 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 section 94B of the Act is suggested as there are also in the business of financing and leasing.

GST Related Issues – Banks, NBFCs, Asset Reconstruction Companies (ARCs)

3.7.17. Provide clarity on exclusion of Securitization Transaction from GST

As per section 7 read with Schedule III of the CGST Act, 2017, Actionable Claims, other than lottery, betting and gambling will neither be treated as a supply of goods nor a supply of services. As per section 2(1) of the CGST Act, 2017 "actionable claim" shall have the same meaning as assigned to it in section 3 of the Transfer of Property Act, 1882. As per Section 3 of Transfer of Property Act "Actionable Claim" means a claim to any debt, other than a debt secured by mortgage of immoveable property or by hypothecation or pledge of moveable property, or to any beneficial interest in moveable property not in the possession, either actual or constructive, of the claimant, which the Civil Courts recognize as affording grounds for relief, whether such debt or beneficial interest be existent, accruing, conditional or contingent. If reference is made to the Transfer of Property Act, due to restrictive definition therein, the secured debt would get excluded from the definition of Actionable Claims and would be subject matter of dispute in future. If GST is levied on actionable claim then it

would severely hamper the business of Banks, NBFCs and ARCs as most of the securitization/assignment deals are backed by collateral and thus secured in nature.

Assignment/securitization transactions are transactions in money and should not be subject to GST. Taxing such transactions would mean either taxing a loan transaction or taxing interest thereon. The treatment of securitization transactions where the underlying asset is secured is not clear under the GST regime. It is pertinent to mention that securitization transaction is strictly governed by the guidelines issued by the Reserve Banks of India from time to time. Securitization transactions mostly happen in respect of priority sector loans and retail loans, which act as an important link to fund the under-served and un-banked population. It is requested that appropriate clarity be provided in respect of securitization transactions under the GST regime. In this connection, it may be noted that countries worldwide like Canada, Malaysia, United Kingdom, Singapore, Australia etc. have specifically kept securitization transactions outside the indirect tax regime.

3.7.18. Exempt Overdue Interest on lending transactions from GST

The notification no. 12/2017 – Central Tax (Rate) dated June 28, 2017 has specifically excluded interest income under Serial No. 27 which read as under "Service provided by way of (a) extending deposits, loans and advances in so far as the consideration is represented by way of interest or discount (other than interest involved in credit card services)" is exempted from GST. In one of the FAQs, it has been further clarified by CBEC that penal interest is a consideration for tolerating an act and it is supply of service and will be taxable. In case of NBFCs, if the borrower defaults in making the repayment on time, the NBFCs charges additional interest for the delay period. This additional amount is interest only and should not be subject to GST. GST on interest income would increase the cost of borrowing and result in inflationary pressure. This cost will have to be absorbed by the businesses as well as by the common man. This would also make Financial Sector including Banks and NBFCs in India extremely expensive in comparison to other countries across the world. It is requested that a suitable clarification be issued by the Government to provide the extension of the exemption provided to interest earned on loans, deposits and advance would even apply to penal/overdue interest.

3.7.19. Categorization of borrower as Registered/ Unregistered and Valuation in case of repossessed Vehicles

The GST law has introduced new provisions for dealing with sale of repossessed assets by a financer. Rule 32 (5) of Central Goods and Service tax Rules 2017, prescribes that in case of goods repossessed from a defaulting borrower who is not registered, GST is required to be paid on sale value less notional depreciated value of the asset as per the method specified. The draft GST Law published on June 2016, had proposed that no GST shall be applicable on the financer in case of sale of repossessed asset belonging to a registered borrower. In such case the intent was to recover the GST from the borrower, as he had taken credit of GST when the funded asset was acquired by him. However, this clause does not appear in the final GST legislation. While the law, as it stands today, has apparently differentiated between registered and non-registered borrowers, there is no difference for the financer as he does not get any benefit of input credit, irrespective of whether a borrower is registered

or unregistered. For the financer, all the modalities of lending, repossessing and sale are similar for both unregistered and registered borrower. Further, the biggest problem is in identifying who is a registered and who is an unregistered borrower. The problem is bigger for existing borrowers, and more so for existing retail borrowers**.** The onus of discharging the tax liability is with Bank/NBFC for both, unregistered and registered borrower. It is accordingly suggested that distinction between registered and unregistered borrowers may be done away with for the specific purpose of sale of repossessed assets and the provisions of Rule 32(5) of the CGST Rules may be extended to registered borrowers also.

3.7.20. Clarification on purchase price of second hand vehicles

NBFCs cater to the financing of used vehicles and face an inherent problem where a formal purchase invoice for such assets may not be available at the time of purchase by the buyer of the said used asset (especially in cases where the sale and purchase is between two individuals). The document that is relied upon is an agreement between the parties or some alternate document such as the valuation report of the asset. Since the purchase price is required for determining applicable GST in case of repossession and sale of financed vehicles in future, a clarification may be provided that the value mentioned in the Loan Agreement or valuation report at the time of purchase shall be considered to be the relevant price and depreciation can be charged on the same for deriving the taxable value of supply.

3.7.21. Exclude trusts from purview of GST regime

The definition of 'Person' includes 'Trust' (as per section 2(84)(m) of the CGST Act). The asset reconstruction business typically operates under various trusts as loan pools are formed into separate trusts for the purpose of isolating the risks and rewards of a set of investors from the others. Accordingly, there are thousands of such trusts that exist under the asset reconstruction sector in India. These ARTs are formed with the purpose of stressed assets resolution and hence do not render any taxable output services otherwise. Inclusion of trusts creates tremendous burden of compliance and increased cost of compliance. It is recommended that asset reconstruction trusts be specifically excluded from the definition of person or alternatively, compliances under GST for ARTs should be relaxed and be shifted to asset Reconstruction Company as a representative/sponsor.

3.7.22. Clarification to avoid ITC reversal on Interest income

As per the provisions of the GST law, interest income is not liable to GST. As per provisions of Section 2(78) of the CGST Act, 2017, non- taxable supply means a supply of goods or services or both which is not leviable to tax under CGST Act, 2017 or IGST Act, 2017. Further, as per Section 2(47) of the CGST Act, 2017, "exempt supply" includes non-taxable supply. Therefore as per combined reading of both the sections, interest would need to be considered as exempt supply for calculation of reversal of ITC as per the provisions of section 17 of CGST Act, 2017. Under the erstwhile indirect tax regime, interest was required to be excluded while arriving at the exempt supply for the purpose of CENVAT credit reversal. Due to inclusion of interest in the purview of exempt supply, cost of doing business will increase tremendously and hamper the business adversely. Therefore, similar provisions

for exclusion of interest income for computing exempt supplies for the purpose of reversal of credit should be provided under the GST laws.

FOOD PROCESSING

3.8.1. Exempt GST on wheat flour put up in unit container and bearing a registered brand name

Flour [1101, 1102, 1105, 1106] Atta, maida, besan etc. [other than those put up in unit container and bearing a registered brand name] are taxed at "Nil" rate of duty under GST whereas, when the identical goods are packed in unit containers bearing a registered brand name the rate of GST has been set at 5%.

In fact, as many as 21 States did not levy any tax, on branded packaged wheat flour under the erstwhile regime. The incidence of VAT on Maida and Atta was prevalent only in a few States in the pre-GST regime. There was no distinction between branded and unbranded products in this category. The average VAT rate was less than 2% and there was no levy of Excise Duty. The levy of GST at 5% will not ensure tax neutrality, given that the value addition is limited and thereby the input credit is also limited. The Government has ensured that all basic household staples, including Branded Bread are kept at taxation levels under GST that are equivalent to or lower than the tax incidence on these goods in the pre-GST regime. In line with this position atta should also be kept at "Nil" rate of GST – more so since roti made from atta is a staple food for Indian households.

Branded Maida or Atta meeting the daily food requirements of ordinary common man should be put under Nil tax structure irrespective of its bearing any brand name or being marketed in a unit container as it only signifies hygienic and quality processing of wheat products meeting the FSSAI specifications and taxation at any stage is bound to add to the cost of the product.

It is recommended that, Flour (Atta, Maida, Besan) put up in unit container and bearing a registered brand name under HSN 1101 should be made liable to nil rate under the GST regime.

3.8.2. Removal of Cess of 12% on Aerated Beverages

It is observed that the principle of maintaining same or near same tax incidence under the GST regime was not upheld when GST tariffs were rollout on 1st July 2017. Below summary indicates that All India Weighted Average Tax incidence on the Aerated Beverages category witnessed an increase of 53% in 3.5 Years:

1st March 2014: 26% (Excise Duty + VAT + Local Body Taxes + Sugar Cess)

1st March 2015: 31% (Excise Duty + VAT + Local Body Taxes + Sugar Cess)

1st March 2016: 33% (Excise Duty + VAT + Local Body Taxes + Sugar Cess)

1st July 2017: 40% gets implemented (GST @28% + Compensation Cess @12%)

GST tax incidence as it stands today for Aerated Beverages is a staggering increase of 7% if we take end of FY 2016 as the reference. As per earlier announced principles of fixing GST

tariffs, financial year 2015-16 was the base year and businesses were assured that there will be minimal changes in the GST regime. However, there is a steep 20-21% rise in tax for the category which is already taxed at a high threshold. And prior to FY 2015-16, there was an increase in VAT in the period 2014-15 made by several States to expand their revenue base in light of the upcoming GST regime. Hence the true tax base for consideration for aerated beverages industry is 26% in the GST regime. In light of the same, it is recommended that compensation cess applied on aerated beverages be reviewed/removed under the GST regime and the rate of GST on aerated beverages be fixed at 28%.

HEALTHCARE, MEDICAL EQUIPMENTS AND DEVICES

I –HEALTHCARE

3.9.1. Increase in Budgetary Allocation

A staggering 70 percent of India's population lives in rural areas and has no or limited access to hospitals and clinics. Nearly one million Indians die every year due to inadequate healthcare facilities. An increase in the budgetary allocation, which will improve the healthcare infrastructure and facilities, is the only way India can fight against diseases. Efforts should be made to increase the public spend on healthcare to 4% of GDP to meet the universal healthcare goals of the country.

3.9.2. Long Term Financing Option for Healthcare Sector

Healthcare was included in the harmonized master list of Infrastructure sub sectors by the Reserve Bank of India in 2012. This includes hospitals, diagnostics and paramedical facilities. Also, IRDA has included healthcare facilities under social infrastructure in the expanded definition of 'infrastructure facility'. In spite of this, long term financing options are still not available for healthcare providers. The Ministry of Health and Family Welfare needs to work out a solution along with the Ministry of Finance to provide long term financing to the healthcare sector. This will channelize funds from the banking sector to create necessary healthcare infrastructure and enable development of innovative long term financing structures for healthcare providers. It will also help in creating an attractive environment for domestic production of medical equipment, devices and consumables as well as catalyzing research and development. Also, the savings that hospitals accrue could be ploughed back to expand hospital bed capacity and facilities which would assist in improvising healthcare services and bed to patient ratio in the country. There is need for long term financing options for the healthcare sector, as provided to the other sectors accorded with the 'Infrastructure Status'. Also, healthcare sector should be accorded 'National Priority' status.

GST

3.9.3. Healthcare Services to be made zero rated

Healthcare services continue to be exempt under GST, as it was under the service tax regime. However, there has been an increase in the rates of tax for inputs and input services consumed by healthcare providers and providers are not eligible to claim any input tax credit. This will result in accumulation of indirect taxes at hospitals and clinics, thereby directly increasing their costs, which will in turn be passed on to the patients. This is not in

line with the stated objective of the Government to provide affordable low-cost healthcare services. It is suggested that "zero rating" of healthcare services be considered, which would ensure that input tax credit is available for refund for the healthcare providers.

Further, the rate of GST on items such as life saving drugs and diagnostic kits, healthcare devices and accessories such as catheters, hospital beds, insurance services, bact alert media (HS Code 38210000), preventive healthcare being considerably high and thus needs to be reviewed by the Government.

DIRECT TAX

3.9.4. Deduction in respect of Health Insurance Premia - Section 80D

Unlike many other countries, India does not have a comprehensive health-care system for its citizens. There are Government hospitals but the facilities available are inadequate while the private hospitals are very expensive. It is suggested that the limit of deduction towards payment of health insurance premium be increased to Rs. 50,000 per annum incentivizing families to seek adequate cover for entire family including parents. The allowance for medical expenditure incurred on senior citizen should be allowed over and above insurance premium allowance. There is a dire need to raise the limit under section 80D of the Act to achieve two-fold objective of giving a tax incentive while also encouraging people to obtain larger healthcare cover in wake of the rising costs. The expenses on preventative Health check-up should also be allowed over and above the Health Insurance Premium to promote Healthy India.

3.9.5. Restoration of Weighted Deduction under Section 35AD

Currently, a weighted deduction under section 35AD of the Act in respect of the capital expenditure (other than land/ goodwill/ financial instrument) is available to a taxpayer engaged in building and operating a hospital with at least hundred beds which has commenced its operations on or after April 1, 2012 – 150% of capital expenditure.

However, with effect from April 1, 2017, deduction under section 35AD of the Act is restricted to 100% of the expenditure only.

Based on the existing dispensation which allows for the weighted deduction scheme, several hospital groups had begun setting up green field capacities and given the long gestation period in identifying suitable land parcels, getting government approvals etc., there are several projects which have taken off but will get completed/commence only in the next 3-4 years. A sudden withdrawal from April 01, 2017 has led to a significant negative impact on the initiatives that have already commenced on these fronts. This move has removed a critical benefit available to the healthcare sector which is already confronted with various other challenges such as contending with spiraling cost of real estate for setting up hospitals, high rate of medical technology obsolescence, shortage of skilled medical resources and long gestation period.

Given the urgent need to add bed capacity in the sector, the 150% weighted deduction scheme should be allowed to continue for the healthcare sector for an additional 5 years at least.

3.9.6. Simplification of the tax regime in respect of Real Estate Investment Trusts (REITs)/Business Trust

Real estate as well as infrastructure companies could have a wide portfolio of assets wherein only a portion is sought to be transferred/is eligible for being transferred to a REIT/INVIT. Amongst different options available for restructuring, one of the alternatives could be to transfer the desired/ eligible assets to a wholly owned subsidiary (with aim to bring it under the REIT/INVIT structure eventually). While Section 47(iv) provides for an exemption from levy of capital gains of capital assets between holding company and wholly owned subsidiary, there is no corresponding exemption provided from levy of MAT on such transfers. When the shares of the wholly owned company (which now house the REIT/ INVIT assets) are swapped for units of the REIT/ INVIT, an exemption is provided for such swap under the normal tax provisions as well as MAT- however, the earlier exemption vis-à-vis levy of capital gains available under Section 47(iv) is lost owning to the subsidiary ceasing to qualify as a "wholly owned subsidiary" prior to expiry of 8 years. In light thereof, it is suggested that (i) The exemption available for transfer of assets to the wholly owned subsidiary should not be withdrawn owing to break in the "wholly owned subsidiary" relationship prior to 8 years if the same is arising as result of transfer to a REIT/ INVIT (ii) Exemption from levy of MAT should also be provided to transfer of assets to the wholly owned subsidiary.

Further, once external investors take a stake in the real estate assets holding company, they would be doing this through a Business Trust structure which gets listed on a stock exchange. The real estate assets holding company would then dividend out returns generated from the real estate assets to the external investors – while doing so there would be incidence of dividend distribution tax on the dividends distributed to the investors as a result of operation of Section 115O of the Income Tax Act. It is suggested that dividend distributed to the external investors be treated as exempt from levy of DDT under section 115O of the Act. The above two measures would accelerate growth and ensure scale, speeds and skill sets for setting up more hospitals which are direly needed given the huge healthcare needs in the country.

3.9.7. Extension of Tax Benefits to Speciality Centres and Hospitals Investing in Substantial Expansion

(i) Extend the benefit of deduction under Section 35AD of the Act to a 50 bedded specialty center which is focused on treatment of Non-communicable diseases ('NCDs').

(ii) The healthcare business by its very nature needs to make continuous investments to upgrade existing capabilities. It is imperative to provide for a tax incentive in terms of substantial expansion to upgrade existing capabilities in an existing hospital. It is recommended that the deduction under section 35AD of the Act may be extended to provide benefits to hospital incurring substantial expansion. The following suggestions are made:-

a) Tax Incentives for promoting Specific Developmental Activities

Tax incentives may be provided for the following activities:-

(i) Digitization - To boost the 'Digital India' initiative of the government, financial incentives/grants should be provided to institutions that are willing to move towards

maintenance of Electronic Health Records (EHR) and Health IT Systems. 250% deduction on investment made for the implementation of EHR should be extended.

(ii) Accreditation - To incentivise hospitals and diagnostic laboratories to undergo accreditation, there should be 100% deduction on approved expenditure incurred for securing accreditation from National Accreditation Board for Hospitals and Healthcare Providers (NABH) and National Accreditation Board for Testing and Calibration of Laboratories (NABL) respectively.

(iii) Remote care - 250% deduction for approved expenditure incurred on operating technology enabled healthcare services like telemedicine, remote radiology etc. should be allowed for improving accessibility, affordability & quality healthcare in remote areas.

3.9.8. Other Incentives:

- Healthcare is a capital-intensive industry wherein very few players are able to generate decent returns. High upfront investment makes the gestation period of the projects extremely longer. Hence, an interest subsidy should be given to make investments attractive.
- Land prices are rising at a tremendous pace and it is exorbitant in the prime location of city. This escalates the project cost and makes it unviable. A subsidy on capital investment would reduce the upfront investment and help generate positive returns faster. Capital subsidy for acquisition of land and construction of hospitals should be provided.
- Access to funding by creating a specific fund for healthcare infrastructure and innovation would facilitate access to capital for the industry. These funds would encourage entrepreneurship and newer business models which are the need of the hour for improving access, availability and quality, especially in Tier 2, Tier 3 and rural areas. The Government should provide the seed capital for such a fund. It is recommended that the government should set up a Health Infrastructure Fund and a Medical Innovation Fund.

II - MEDICALEQUIPMENTS, IVDs AND MEDICAL DEVICES

GST

3.9.9. Reversal of input tax on issuance of goods free of cost and destruction of expired goods

In the healthcare sector, it is a common practice of supplying devices/ equipment/consumables to customers (hospitals, doctors, physicians) on a 'demo/ sample trial' to familiarize and acclimatize with the product before the same are procured in the course of or furtherance of business and moreover Healthcare practitioners fraternity across the world are of firm believer to have trials before placing any order since it impacts patients. In absence of demonstrations and sample consumables, sales of high-value medical equipment's will not be possible and it is a necessity for the Industry to have demo equipment available at Doctors/Hospital (Customer) Sites before any purchasing decision is made by them and to provide them opportunity to try products before they can actively

recommend these to their patients at large. Considering that these devices/equipment/consumables are merely provided to the customer for demo/ testing purpose and are not intended for sale, they should not be subject to input GST reversal, failing which, every time that these demo/free trials are given input GST would have to be reversed and the overall tax cost in the system would go up without any corresponding economic benefit/commercial transaction. The cost of demonstrations and free samples, being inherent to the medical devices and implants, are already built into the final selling prices of finished goods that are sold against payment of GST. It is therefore suggested that requirement of reversal of input tax credit on free trials and samples distributed in the course of business be dispensed with.

Medical devices best practices require the manufacturer/distributor etc. to safely dispose of the expired goods to avoid misuse or adverse impact on the health of patients and therefore at times, they have to take back expired items from the trade channels. Most of these device, implants and consumables have a shelf life between 1-5 years, which also determines the return window range similarly. Accordingly, it is imperative upon the suppliers to keep adequate stocks during product shelf life to meet twin objectives of minimizing avoidable inventory destruction costs in the distribution chain while simultaneously maintaining sufficient supplies meeting the patient requirement. It is accordingly recommended that an appropriate amendment be made in the GST law to provide that reversal of input tax credit on expired goods as per section 17(5)(h) of the CGST Act, 2017 will not apply to the healthcare industry.

3.9.10. Review of rates under GST regime on products under HSN 9021

The rate of GST of 12% as applicable on products under HSN code 9021 (which attracted nil rate of CVD) is very high. This chapter covers products such as Orthopedic Appliances, Including Crutches, Surgical Belts and Trusses; Splints and Other Fracture Appliances; Intraocular Lenses, Artificial Parts of the body; Hearing Aids and Other Appliances which are worn or carried or implanted in the body, to compensate for a defect or disability. The increased tax under GST raise healthcare cost for the patients and needs to be corrected at the earliest.

3.9.11. Rate of GST on Contact Lens disinfecting solution to be at par with rate of Contact Lens

The applicable rate of GST on Contact Lens disinfecting solution (HSN 3307) is 18% whereas the GST rate for Contact Lens (HSN 9001) is 12%. The Lenscare Solution, which acts only as a disinfectant to protect Contact Lens, has been charged higher (18% GST) than contact lens (HSN9001). Essentially, Lenscare Solution is used only by Contact Lens users, where Contact Lenses have a GST rate of 12% and therefore lenscare solution should also be grouped in the same rate bracket, as otherwise, this is leading to the overall cost of the consumer being higher. Many of contact lens is also used for therapeutic purposes to treat corneal blindness like in the cases of Keratoconus (highly prevalent in India), corneal scarring etc. Considering these facts, the Contact Lens and Lenscare solution should have preferential GST rate of 5% only to help grow penetration for this category.

3.9.12. Review of rates under GST Regime for Dialysis Consumable

Dialysis Consumables being used for treatment were having lower tax rates under pre-GST regime, however higher tax rates under GST regime are resulting in dialysis treatments being unaffordable to the population affected with End Stage Renal disease (ESRD). In many of the scenario this cost pressure would compel service providers to compromise on the treatment quality and encourage reuse practices of consumables misaligned with the vision of Affordable, Accessible and Available dialysis treatments under National Dialysis Program. The following data validates the above hypothesis:-

Consumable	*Pre GST Tax (%)	Post GST Tax (%)
Blood Tubing	0	12
Dis infectant	5	18
Bibag	5	12
Fistula Needle	0	12

It is recommended that since these products are the part of overall dialysis process, therefore these products should be exempted from GST. For example before GST implementation, dialysis consumables were exempted from Taxes in Maharashtra making dialysis treatments affordable solutions to renal patients.

Further, clarity is required on HSN codes and rates applicable to Dialysis Machines.

3.9.13. Correct classification of IOLS under tariff heading 9021 from tariff heading 9002

As per the schedule of rates under GST regime, Intraocular Cataract Lenses (IOLs) were classified under tariff heading 90213900, subject to GST @12%. This classification was in conformity with the erstwhile HSN Customs Tariff Heading of 90213900 for IOLs.

Subsequently, the GST Schedule of approved rates for goods was revised on 11 June 2017, wherein IOLs were continued to be taxed at 12%, however, IOL's were classified under the chapter heading of 90029000 vide Notification No: 1/ 2017 CGST dated 30 June 2017. The IOLs seems to be inadvertently classified under tariff heading 9002 instead of CTH 9021. It is requested that appropriate amendment be made wherein tariff heading of IOLs may be amended back to 90213900 under GST in line with the CTH and facilitate clearance of IOLS at correct international classification and duty rates.

CUSTOMS

3.9.14. Reduce custom duties on medical devices

There has been substantial increase in custom duty on medical devices (items falling under HSN 9018 and 9021). This has adversely impacted costs for these products in India where the Government agenda is to provide low-cost healthcare available to masses. This is especially important in view of the fact that a significant 67-70% of healthcare spends is through private spending and there exists a wide gap in local manufacturing of high-quality medical devices. It is recommended to restore the import duty rates on medical devices to earlier rate of 5% import duty (BCD) where the overall import duty costs were within range

of 5% -10% and commensurate with import duty rates in other competing economies like Singapore, Malaysia, Hong Kong, Indonesia etc.

DIRECT TAX

3.9.15. Allow Depreciation on CT Scan Machine @ 40%

Income Tax Rules, 1962 provides rules of depreciation on life savings medical equipment eligible for depreciation @ 40%, however, the name of CT Scan Machine is not mentioned. CT Scanner is also a lifesaving machine hence should be eligible for depreciation @ 40% under the block of life saving medical equipment.

III- LIFE SCIENCES

GST

3.9.16. Requirement to reverse ITC on distribution of Physician Samples be done away with

Supply of physician samples to the doctors are an integral part of the Pharma Industry and important for providing the medical practitioners of the knowledge of the products/its benefits to patients. In terms of Section 17(5) (h) of the CGST Act 2017, ITC in respect of free samples is not eligible. It is suggested that supply of physician samples should not be subject to reversal of credit. Further, clarity with respect to the procedure for movement of date expired medicines from the chemist/distributor to the manufacturer for destruction be provided under GST regime.

3.9.17. Allow ITC in respect of control samples

Every batch/lot of each drug product manufactured is required to be sampled. These samples in trade parlance are referred to as 'Control samples'. Control samples are maintained in the factory for a specified time, after which they are destroyed. It is salient that maintaining and destroying control samples is a legal requirement and hence mandatory for the manufacturer. In terms of Section 17(5) (h) of the CGST Act 2017, ITC in respect of goods destroyed is not eligible. As maintaining and destroying control samples is a legal mandate, it is suggested that ITC in respect of control samples should not be denied. Appropriate amendment be made in the law to allow claim of ITC for such situations.

3.9.18. Provide exemption from requirement of Delivery Challan

Under the provisions of the GST law, goods sent by Principal to Job-worker must be under a cover of a Delivery Challan, including cases where the goods are directly sent to Job-worker. In cases where the third party sends the goods to Job-worker directly on the directions of Principal, it is practically impossible that the Delivery Challan issued by Principal can accompany the said movement of goods. In the pharmaceutical industry, the job-work process works along a loan licensee model, wherein the goods are directly sent by suppliers to the job-worker. Due to the requirement of a Delivery Challan to accompany such goods, the operationalization of the loan licensee model is becoming practically non-workable. Accordingly, it is suggested that the requirement of Delivery Challan to accompany the movement of goods in case of direct supply by third party to Job-worker should be

removed. In such cases, Delivery Challan may be allowed to be issued by Principal to Job-worker once the goods are actually received by job-worker.

3.9.19. Provide exemption from GST on clearance of products for testing

In the Pharma Industry, products for testing (popularly known as 'testing samples') are sent to Contract Research Labs/ Organizations (CROs). Such testing samples are sent for bio-equivalence studies between own development product and the innovator product to validate against certain defined technical parameters. Samples which are sent out for testing often do not come back to the plant from where they are originally dispatched, as such samples are consumed in the process of testing. CROs or R&D Centres, as the case may be, issue a Test Report which is submitted to the regulatory agencies [like US Foods & Drugs Administration (USFDA) etc.] to validate the drug development process. Supply of testing samples to CROs should not be considered as 'supply' under GST law and hence not chargeable to GST. Further, since these samples are not distributed as 'free samples', ITC may not be required to be reversed. It may be noted that the third party CROs charge the manufacturers for the testing and analysis services provided, along with applicable GST. It is requested that necessary clarification be issued in this regard to avoid any litigation in future.

DIRECT TAX

3.9.20. Weighted Deduction under Section 35(2AB) for computing Book Profits

Presently, while computing the 'book profit' under Section 115JB, the amount of weighted deduction under Section 35(2AB) is not deducted. In order to promote in-house R&D in India, the amount of weighted deduction under section 35(2AB) of the Act should be deducted while computing book profit for the purpose of MAT.

3.9.21. Safe Harbour Rules for Contract Manufacturing

The Central Board of Direct Taxes has notified Safe Harbour Rules covering sector like IT/ITES, KPO and Auto Component manufacturer prescribing desirable margins to avoid litigation on transfer pricing matters.

It is requested that similar guidelines for pharma companies that are manufacturing and exporting the product as contract manufacturer be provided.

3.9.22. Provide weighted Deduction under Section 35(2AB) for Clinical Trials

The current provisions for deduction under section 35(2AB) of the Act covers only expenditure incidental to research carried on at the in-house R&D facility. As clinical trials are specialized and expensive most R & D facilities outsource these trials. Hence, in order to successfully launch any new drug, the innovator has to get the clinical trial done outside approved facilities within India & abroad. Therefore all expenditure related to research i.e. clinical trials, bioequivalence studies, regulatory and patent approvals should be eligible for weighted deduction, even if these activities are carried outside the approved R&D facility. Presently, as per Department of Scientific and Industrial Research (DSIR) guidelines amount spent by a recognized in -house R&D towards foreign consultancy, building maintenance, foreign patent filing are not eligible for weighted deduction under section 35(2AB) of the

Act. DSIR guidelines need to be modified accordingly to allow the above said expenses for weighted deduction under section 35 (2AB) of the Act. It is further suggested that weighted deduction under section 35(2AB) of the Act should be enhanced from existing 200% to 250% for a period of next 10 years i.e. up to 31st March, 2024.

HOUSING & REAL ESTATE

DIRECT TAXES

3.10.1. Deduction of Interest paid on Borrowed Capital

The deduction available under section 24 of the Act is to a maximum limit of Rs. 2,00,000/- for interest on loan taken for acquisition/construction of self-occupied house property. Given the rising interest rates and the increase in property prices and also to spur the demand for housing, it is recommended the exemption should be increased to at least Rs. 3,00,000/- per annum.

Currently interest paid on home loan during the period of construction is allowed as deduction in five yearly instalments starting from the year in which the construction is completed and the taxpayer claims possession of the property. Often completion of construction of the property is delayed due to extraneous reasons not entirely within the control of the taxpayers. Many taxpayers have to pay interest on the home loan and additionally rent till the property is ready to occupy. This may leave many taxpayers with very little cash for other expenses. Non-deductibility of housing loan interest paid in the respective years during the construction period also has another challenge. Maximum home loan interest which can be claimed as loss on self-occupied property is Rs. 200,000. Also, in respect of let out property the loss cannot exceed Rs. 200,000 after deducting municipal taxes and standard deduction of thirty percent on the net amount. With the skyrocketing prices of the housing property, this threshold limit of Rs. 200,000 would often be insufficient even to cover the current year interest, leave alone one-fifth share of pre-construction interest. Even in case of let-out property the rental income during the earlier years would be significantly lower and in most situations the loss on house property will far exceed Rs. 200,000 even before considering the pre-construction interest.

It is recommended that section 24 of the Act be amended to provide for a separate deduction so that the preconstruction interest is allowed in five instalments without any threshold limit. Similar amendment is also required in sub-section 3A of section 71 of the Act to allow setoff of loss from house property in excess of Rs. 200,000 to the extent the excess amount represents pre-construction interest.

3.10.2. Taxability of Immovable Property received for inadequate consideration

Section 56(2)(vii)(b) of the Act provides that receipt of immovable property by an individual or HUF for a consideration which is less than stamp duty value of the property by more than Rs. 50,000, will be taxable as income from other sources to the extent the stamp duty value is in excess of the consideration. The provision levies tax on inadequacy of consideration. Section 50C/43CA of the Act deals with such inadequacy in hands of the seller/ transferor. Section 56(2)(vii) of the Act will tax the same inadequacy in the hands of the purchaser as

'income from other sources', where sale consideration is less than the stamp duty of the property by an amount exceeding Rs. 50,000 as stamp duty value less consideration. Both, seller and purchaser, pay tax on same inadequacy of consideration and thus, there is double taxation to that extent.

It is recommended that clause (ii) to Section 56(2)(vii)(b) of the Act should be deleted as it will lead to double taxation, which could not be the intended objective of the Government.

Alternatively,Section50C/43CAoftheActmayneedtobecorrespondinglymodifiedtoexcludesuch transactionwhich has been taxed under Section 56(2)(vii)(b) of the Act.

It is also observed that in the continued sluggish market conditions, this section is a big deterrent for real estate developers as circle rates fixed by the State Government in many cases are higher than the market value or the value negotiated by and between the seller and buyer. It is pertinent to observe here that many State Governments have notified reduction in Circle Rate after review and assessment of the ground situation. In consequence thereto, this makes seller and buyer both liable to pay tax on notional gain or profit under the provisions of section 43CA, 50C and section 56(2)(vii)(b) of the Act making the case for double taxation. It is recommended that the provisions of these sections be reviewed in light of the actual situation.

HYDROCARBON

GST

Petroleum products are an input to many industries and commercial activities. GST being applicable on the final product and not on the petroleum products which are inputs to the value chain defeats the purpose of GST.

Natural Gas being a cleaner fuel and the loss of tax revenue is not significant. So Natural Gas must be immediately put under the GST ambit.

3.11.1. Inclusion of Petroleum & Natural Gas within GST framework (including regasified LNG)

Petroleum products directly enter as an input into a large number of economic activities (e.g., transportation, electricity generation and fertiliser production). Apart from such direct uses, there are a number of indirect uses as well. Therefore, changes in prices (or taxes) of petroleum products would have a significant impact on the economy both through direct as well as indirect or cascading routes. The cascading overall impact on the other core sectors which are critical will be such that it would seriously impact the manufacturing competitiveness of India. Thus, increase in tax incidence would not only increase the Capital Cost of the Oil and Gas Sector but will also have an inflationary impact on the economy. In view of the above-mentioned adverse impact for non-inclusion of the Petroleum Products in GST regime, our request is as follows:-

Option 1: Petroleum Products be included in the GST regime

All petroleum products such as petrol, diesel & natural gas should be immediately brought under the ambit of the GST regime. Non-inclusion of the same has pushed up costs for the

sector. No input credit is available on goods and services used for petroleum operations. Denial of credits has resulted in massive cascading impact and increased cost of production placing the domestic industry in a competitive disadvantageous position. This has an adverse impact on investments in this sector which is critical for energy self- sufficiency and import substitution.

It is recommended that oil and gas be included in GST regime, and thus, GST is levied on sale/supply of oil and natural gas. This inclusion will provide free-flow of credit and avoid cascading impact.

Option 2: Petroleum sector/Oil and Natural Gas sector may be accorded a status of zero-rated goods under GST regime

The Government may consider to grant the zero rated goods status to Oil and Gas industry. The zero-rated status should allow this industry to claim a refund of GST paid on procurement of goods and services.

Option 3: Petroleum sector/Oil and Natural Gas sector may be charged a nominal rate of GST

Charging of nominal rate of GST on the output of Oil and Gas industries will enable these companies to avail the credit of input GST credit therefore avoiding stranding of costs.

3.11.2. Reversal of input credit relating to Non-GST supplies be made nil

The provisions of the GST law require reversal of input tax credit in respect of exempted/non-taxable supplies. It would be unfair to compel a company to lose common credit merely because it has (non GST) trade turnover which may be more than 10 times higher than a service income merely for the same unit of measure due to the cost of the traded goods. This cost is of traded goods is not a value add of a trader and therefore should be excluded from the definition of turnover for comparing with a service income. This is akin to comparing the price of an air conditioner with the installation charges of an Air Conditioner by an AC dealer to its customer and denial of common credits on business costs of the AC Dealer. What is more reasonably comparable is the margin made by the dealer on the sale of the Air Conditioner with the installation charges for the Air Conditioner. From a combined reading of the various provisions of the GST Act it is evident that:-

- the exempt turnover includes non GST leviable category i.e. the petroleum goods
- turnover as it stands in the bill includes the cost of traded goods for a trading entity.

It is also being pointed out that including the petroleum goods as exempt category is unfair as VAT and Excise duties etc. continue to be applicable taxes on the manufacture and sales of these products. It is accordingly suggested that petroleum goods (being taxed separately) be excluded from the purview of exempt and total turnover under the GST laws for the reversal of credit.

3.11.3. Exemption from GST on import of vessel

In energy sector, vessels, tugs, barges etc. are imported by upstream companies or its vendors i.e. sub-contractors into India under charter-hire arrangements for specific period

of lease. Import of vessel was exempted from payment of whole customs duty subject to Essentiality Certificate (EC) issued by Directorate General of Hydrocarbons (DGH). Under GST regime, though Basic Customs Duty and Customs Cess continues to be exempted, IGST of 5% is made applicable in terms of Entry no. 404 of Notification No. 50/2017 – Customs, dated June 30, 2017. In view of this Notification, IGST of 5% stands applicable on the assessable value of vessel, barge or tug at the time of its importation. In case where such vessel, tug or barges are imported by operators, sub-contractors or other vendors, such upfront payment of IGST @ 5% on assessable value of vessel, barge or tug leads to huge blockage of cash-flow for all importers. Also, in case where vessel, tug or barges are imported by sub-contractors or their vendors for shorter period of contract, the importers would not be in the position to claim credit of IGST paid since there would not be sufficient output GST liability. Such importers would be mandatorily required to opt for drawback or export the same on payment of IGST and claim refund of the same. Import of vessel was exempted from payment of whole customs duty subject to EC issued by DGH in the Pre GST regime vide notification no. 12/2012- Customs. Such additional compliance coupled with huge blockage of cash-flow has already impacted operations of oil & gas companies. Further, where the same are imported by upstream companies, the amount of IGST paid less Drawback shall be a cost, leading to increased tax cost for oil & gas upstream sector. In case where vessel is imported for lease period of more than 18 months, drawback is also not admissible. It is suggested that Notification No. 50 / 2017 – Customs be amended to provide for complete waiver of IGST on import of all goods required for petroleum operations including tug, vessel and boats.

3.11.4. Exemption for O&G upstream companies for movement of goods from shore base to offshore

In case of oil & gas upstream sector, goods procured and kept at shorebase are supplied to offshore platforms as per indent. Subsequently, the same goods are supplied back to shore on real time basis on account of non-utilization/space constraint at offshore platforms. Again after few days/weeks, the same goods are required at offshore. Shorebase supplies the same goods to offshore again where IGST was paid during 1st dispatch. Under GST regime, shorebase and offshore location are distinct persons. Hence, on the basis of law, as it stands today, supplies from shorebase to offshore location would attract IGST. Hence, shorebase and offshore locations are required to issue tax invoice and pay IGST on its supplies to offshore location/shorebase, as the case may be, at the time of each supply.

Given this, such levy of IGST on supply of goods from shorebase to offshore location and backload therefrom should be exempted. Alternatively, in case where no upfront exemption is granted and first supplies from shorebase/offshore location are subjected to IGST of 5% once post introduction of GST, further supplies thereof from shorebase to offshore and backload therefrom to shorebase should be exempted without requiring reversal of credit. Such benefit of exemption if not conferred on such subsequent supplies between the same taxable persons i.e. shorebase and offshore platforms would mean levy of GST time and again on the same set of goods.

3.11.5. Admissibility of credit for O&G upstream companies – offshore registration in respect of goods being supplied back to shorebase after its use

In oil & gas sector, there would be multiple movement of goods from shorebase to offshore location and viz versa. Basis current legislation and credit mechanism on GSTN, it seems that offshore locations may not be allowed to claim credit of GST charged by shorebase since goods are used in exploration of oil & gas, which is outside the ambit of GST. Given this, while offshore locations may not eligible to claim credit of IGST charged by shorebase, offshore locations may be burdened with GST once again at the time of backload without credit. Such inconsistency would result into levy of GST again on the same goods as and when they are supplied from shorebase to offshore and loaded back to shorebase. Further, such situation is against the principle of seamless flow of credit.

Option 1: Such levy of IGST on supply of goods from shorebase to offshore location and backload therefrom should be exempted.

Option 2: Alternatively, in case where no upfront exemption is granted and first supplies from shorebase/offshore location are subjected to IGST of 5% once post introduction of GST, further supplies thereof from shorebase to offshore and backload therefrom to shorebase should be exempted without requiring reversal of credit. Such benefit of exemption if not conferred on such subsequent supplies between the same taxable persons i.e. shorebase and offshore platforms would mean levy of GST time and again on the same set of goods.

Option 3: Offshore platforms should be allowed to claim credit of GST charged by shorebase to the extent of goods being back-loaded to shorebase. At times, the goods supplied to offshore platforms are returned to shorebase after lapse of considerable period. In such scenario, credit should continue to be allowed irrespective of its time limit.

3.11.6. IGST implications on disposal of excess or obsolete stock

As per Customs Notification No. 50/2017 – Customs read with Notification No. 3/2017 – IGST, tax payers are required to pay GST on depreciated value of goods subject to maximum depreciation to the extent of 70%. The said depreciated value needs to be computed by reducing prescribed percentage for each quarter of usage from its original price. Such mechanism requiring payment of GST at the time of disposal of excess/obsolete stock is not in line with the decision of the courts. Notwithstanding the above, even if GST is made payable at the time of disposal, the methodology to arrive at depreciated value from original purchase price for the purpose of payment of GST has been prescribed without appreciating the ground reality. The goods intended to be disposed of are typically purchased/imported 5 to 10 years back. On other hand, in terms of all indirect tax legislations, maximum time period for maintaining the records is five years.

It is not possible for tax payers to maintain invoices/bill of entry in respect of goods purchased before five years. Hence, the process of arriving at depreciated value by reducing purchase price by prescribed percentage is highly cumbersome. It is not possible for tax payers to correlate each goods being disposed-off with its original bill of entry or purchase invoices after lapse of several years. Additionally, the value derived from sale of such

unutilized surplus goods are at the scrap rate and payment of duty at 30% of import value makes the entire transaction revenue negative. It is recommended that the levy of customs duty (including IGST) should be withdrawn on disposal of surplus/obsolete/used goods.

It has also been observed that the customs authorities have been issuing show cause notices to demand customs duty on surplus goods which have not been used for oil and gas exploration. This issue remains under litigation inspite of a favourable Supreme Court decision in case of Clough Engineering. Accordingly, a clarification may be issued to end the litigation on this matter.

3.11.7. Exemption Notification be extended to "All Goods and Services used for Petroleum Operations"

Notification No.3/2017-Intergrated tax (Rate) and Central tax (Rate) and State Tax (Rate) dated 28th June, 2017, cover only 24 items that would be subjected to Goods and Services Tax (GST) at the concessional rate of 5%. It may be noted that there is no distinction between goods and services as all the services (including capex expenditures services like drilling, cementing etc.) are utilised for carrying out exploration and production of oil and gas only. Exclusion of services from the exemption notification would be prejudicial to the interests of the oil industry and goes against the basic principle behind levy of GST**.** It is suggested that the exemption notification in this regard be suitably amended thereby enlarging the scope of the items to "all goods and services used for petroleum operations".

3.11.8. Provide clarity on rate of GST applicable on time charter vessel

Oil manufacturing companies avail the services of vessel on time charter from ship-owner for transporting petroleum products. There is no clarity as to whether the time charter services rendered by the ship owners by way of charter hire of ships falls under Service Accounting Code 996602 attracting a rate of 18% or under the Service Accounting Code 997311/997319 attracting the rate of 5%. It is suggested that appropriate clarity be provided in this regard.

CUSTOMS AND EXCISE

3.11.9. Include natural gas and RLNG as 'Declared Goods'

Presently there is varying Value Added Tax (VAT) on Natural Gas, including RLNG, across the country. Under Chapter IV (section 14) of Central Sales Tax (CST) Act 1956, which deals with 'Goods of special importance in inter-state trade or commerce', fuels such as coal and crude oil have been notified as 'Declared Goods' on which sales tax of more than 5% cannot be levied in any state irrespective of where the product is sold. Natural gas or re-gasified, both natural gas and LNG should fall in similar category as coal and crude oil. The biggest impact of declaring Natural Gas as a declared good would be on economic development of small on-land and isolated fields. A large number of such fields awarded under New Exploration Licensing Policy (NELP) block remain unattractive due to high local sales tax. Reduction in tax will directly impact the cost of piped natural gas. In addition, lower tax will reduce large subsidy burden on these products. Declared goods status will also make imported LNG cheaper, and thus relatively more affordable for local industries. Further, use of natural gas

in transportation would significantly reduce pollution. It is suggested that the Government may treat RLNG/Natural Gas as a "declared good" so that they have a common concessional rate of VAT.

3.11.10. Exemption from Payment of Customs Duty on Import of Liquefied Natural Gas (LNG)

LNG is a clean fuel and mainly used in fertilizer and Power sector. Recognizing the shortage of gas, Government has encouraged import of LNG. Since LNG falls in the same logical category as Crude Oil, they must have the same level of taxation as applied to Crude Oil. The benefits of using LNG are far-reaching vis-a-vis the revenue loss to the exchequer. International LNG prices are at least 20-25% lower than the Crude Oil (or petroleum fuels) on heat equivalent basis and thus, reduces the cost of energy to end-consumer in addition to the Forex saving.

Since customs duty on crude oil has already been made zero, import of LNG presently attracts Basic Customs Duty of 2.575 % ad valorem which adds to the cost of supply to end-users. Through Finance Act 2012, Government has exempted levy of Customs duty on import of LNG for Power Sector. However, this exemption should be extended to other sectors also. Many countries have exempted custom duty on import of natural gas, for example Argentina, Brazil, Mexico, USA and Norway.

3.11.11. Exemption of Excise Duty for compression of natural gas into Compressed Natural Gas (CNG) for use in Natural Gas Vehicles (NGVs)

Compression of natural gas for supplying to the vehicular segment entails change of mass density in order to increase the storability. Hence conversion of natural gas to compressed form is only for the purpose of transportation and should not be considered as manufacturing, thus excise duty should be exempted on CNG.

3.11.12. Activity of LNG loaning and borrowing in quantity terms in LNG terminals handling should be out of purview of taxable transactions

For the purpose of transportation, natural gas is liquefied to -160 Degrees for ease of handling. This liquefied natural gas or LNG is transported and stored in special vessels and storage tanks that are heavily insulated in order to maintain the temperature of LNG. Natural gas is sold in energy units of the contents thereby making it widely tradable without determination of its physical characteristics or source of supply etc. However, due its transmission over high seas from countries around the world, the supply happens in ship loads the schedule of which cannot be accurately determined. LNG Storage Tanks are also expensive to build and maintain due to the safety challenges of dealing with a high energy content of the natural gas in its liquid form.

These LNG storage tanks are used to store the goods of various parties with virtual segregation of title stocks. However, due to limited storage space, there are situations where demand exists with a certain entity while the title of LNG stock in the Tank is held by another entity resulting in mismatch and restriction of free trade and commerce of LNG in

India, i.e. LNG is available in the Tank, there are willing customers at the gate but the LNG cannot be supplied to them.

The Indian entities are apprehensive of stretched application of laws like 'Right to Use of Goods', rules of barter etc. and thereby hesitant to freely carry out loan/borrow of in tank LNG so as to enable transfer of goods to that entity which has the demand orders in hand. Exemption from any taxing provision for Loan/Borrow transactions of In Tank LNG to enable optimum utilisation of LNG Terminal facilities in India should be specifically provided to facilitate higher trade and consumption of this carbon efficient fuel by India entities.

3.11.13. Zero Customs Duty for new Refineries/Refinery Expansions and other Imports

Zero customs duty should be introduced for the capital goods imported for the new refineries as was extended to RPL Refinery, instead of the current rate of duty of 21.5% (viz. 3% customs + 18% GST) so as to provide a level playing field to the new refineries of the PSUs. It is also suggested that the Customs duty on import of material viz. pipes, valves, flanges, data communication system for laying of petroleum products and gas pipelines is made nil.

3.11.14. CENVAT Credit on National Calamity Contingency Duty (NCCD)

Presently NCCD (National Calamity Contingency Duty) of Rs.50/MT is payable on the indigenous as well as on the imported crude. Even though the same is cenvatable, it can be set off only against payment of NCCD, making the CENVAT credit virtually Nil both to the producer and consumer of crude. NCCD should be made cenvatable against the duty on the finished petroleum products.

3.11.15. Exemption in respect of additional duty levied on High Speed Diesel (HSD)

HSD/Light Diesel Oil (LDO) is continuously required for running offshore supply vessels and rigs as a fuel. Additional duty of excise is levied on HSD @ Rs.6 per Ltr. which adversely affect the fund flow of the Exploration and Production ('E&P') companies. Since goods required for petroleum operation have been exempted from all other customs and excise duties (provided supplied under International Competitive Bidding) additional duty should also be exempted. It is accordingly suggested that the respective notifications be amended to extend the exemption in respect of additional duty of excise levied on HSD.

3.11.16. Permit Mixed Bonding in Intermediate storage tanks for Aviation Turbine Fuel (ATF)

The Central Board of Excise and Customs has after withdrawal of the warehousing provision has permitted establishment of the intermediate storage locations for storing of Bonded ATF. However, no mixed bonding of the bonded and duty paid ATF is permitted in such intermediate storage locations. This puts enormous operational constraints particularly in places where there are limitations on the availability of the storage tanks. Mixed storage of duty paid and non-duty paid goods at Aviation Fuel Station (AFS) at airports has been permitted by the board considering the difficulties in installing multiple storage tanks (separate for domestic and export clearances) at the site of the airport due to space constraints. The permission has been granted subject to the condition that a tank-wise

regular account shall be maintained about the receipt and discharge of duty paid and non-duty paid stocks of ATF. It is suggested that the same facility allowing mixed storage of bonded and duty paid ATF be extended to the intermediate storage tanks. Segregation of the duty paid and bonded ATF can be maintained through accounting records.

3.11.17. Excise Duty on transit Loss on ATF

With the withdrawal of warehousing provision vide notification no. 17/2004-CE dated 04.09.2004 no movement from the refineries can be done without payment of duty. However, in terms of circular No. 804/1/2005-CX dated 4th January 2005 the duty has to be paid on the quantity at the time of clearance from the refinery, and therefore duty has to be paid on the quantities lost in transit or storage after its clearance from the refinery. Further as regards the clearance of ATF to be ultimately supplied to foreign going aircraft it was specified that though ATF can be removed for an export warehouse without payment of duty but no abatement will be allowed as regards the storage losses suffered during the storage of ATF either at intermediate storage location or at export warehouse. Such losses are treated as diversion for home consumption and duty leviable along with interest at the rate of 24%. These losses occur because of the peculiar nature of petroleum products which expands with the rise in temperature and contracts with the fall in temperature and which are beyond the control of refineries and occur purely because of natural causes. It is accordingly suggested that allowance should be given for the quantities lost in transit or storage.

3.11.18. Processing of Excise Duty refund claims

Currently where movement of bonded stock is not possible, duty paid stock is supplied to foreign going airlines and duty refund is claimed. This process takes inordinately long delay. It is suggested that access should be given to online refund process for quick processing with online Real Time Gross Settlement (RTGS) refund.

Miscellaneous Issues

3.11.19. Reduction of percentage of Oil Cess to 10%

The Budget 2016 has amended provisions to levy Oil Cess on the basis of ad-valorem basis instead of fixed rate per MT. It is believed that the percentage of cess should be reduced to 10% to boost the oil and gas sector. The rate of oil cess should be reduced to 10% from 20% in order to boost oil and gas sector.

3.11.20. Clarification on non-applicability of service tax and GST on cost petroleum under erstwhile indirect tax regime and GST regime

Companies have received correspondence from departmental authorities with regard to service tax demand on cost petroleum treating the cost petroleum as consideration paid by government to exploration companies for mining services undertaken by them. The arrangement of Production Sharing Contract (PSC) is such that it invites exploration companies to undertake exploration for itself in conjunction with Government of India. The authorities are demanding service tax on the activity of exploration without appreciating the rationale of PSC. There is no activity carried out by the Government/ Contractors and these

are not consideration for a service but simply a share of the government in the production. Internationally, Profit Petroleum/ Cost Petroleum are not considered as 'service' by the Governments to O&G companies or vice versa and nowhere in the world are indirect taxes applied on such transactions. Clarification should be issued under the erstwhile regime as well as under GST regime that Profit Petroleum/ Cost Petroleum is not consideration for service; these are formulas to determine the Government's share in the production (tax paid sales revenue).

3.11.21. Clarification on non-applicability of service tax and GST on cash calls under the GST regime

A Circular No. 179/5/2014-ST dated 24 September 2014 was issued regarding applicability of service tax on cash calls. However, the said circular has kept the issue open for interpretation of service tax authorities. Given this, recently, oil and gas companies are burdened with demand of service tax on cash calls. It is therefore requested that a clarification should be issued under existing regime as well as GST regime that consortium and parties to consortium (which has executed a sharing agreement with Government of India) are not distinct entities and the cash calls are not consideration for services but only a contribution made by contractors. It is suggested that appropriate clarity be provided with regard to non-applicability of service tax under the erstwhile regime and GST under the GST regime.

DIRECT TAX

3.11.22. Offshore Installations to be included as 'Qualifying Ship' - Section 115VD

As per section 115VD of the Act, qualifying ships are ships registered under Merchant Shipping Act, 1958 with valid certificate of its net tonnage subject to exclusion list which features 'Offshore installations'. Indian EPC contractors operating in upstream hydrocarbon sector, to cater to the upstream offshore oil & gas industry formed a company owning a self-propelled offshore construction vessel operating in Indian and foreign waters, helping EPC contractors to construct complex hydrocarbon platforms. The ambiguity on the applicability of tonnage tax scheme to vessels used in the construction of offshore platforms has resulted in denial of tax benefit under Chapter XII-G of the Act to the company and is under litigation. The intention behind introduction of Tonnage Tax is to link shipping company's tax liability to tonnage of its fleet rather than the profits generated by its commercial operations and thereby promote the industry. In case of construction vessels used for construction of offshore installations like platforms, pipelines etc. income is influenced by tonnage capacity of the vessel and since tonnage is the indicator, it should be legitimately eligible for tonnage tax regime. It is therefore suggested that ships used for construction of offshore installations should qualify as 'Qualifying ship' under section 115VD of the Act and appropriate amendment be made in the provisions of the Act. Inclusion of vessel used for offshore installations in the definition of 'qualifying ship' which are registered under Merchant Shipping Act and accordingly tonnage tax scheme will go a long way in promoting companies who have given the country its first construction vessel (self-propelled and meeting all attributes of Qualifying Ship) and has contributed to upstream offshore oil & gas segment.

3.11.23. Introduce Safe Harbour Rules for LNG Imports

Today, long term pricing for LNG is being replaced by spot prices which are largely determined by a number of instantaneous factors. Nearly 25% of LNG globally is now traded on the spot market. Functions here often involve the identification of potential spot purchasers, agreement with potential counterparties, and range of intermediary logistic services. Further the challenges of accommodation of re-gasification and trading prices, wherein determining safe harbour ad hoc can be extremely challenging. It is recommended that safe harbour rules for LNG imports be provided based on actual dispersion of custom import prices as it will help reduce litigation on transfer pricing of LNG imports.

3.11.24. Non-Use of Secret Comparables for Pricing of LNG

The term secret comparable denotes a comparable whose data is not available in the public domain but is known only to the tax authority which is making the transfer pricing adjustment. Determination of Liquefied natural gas (LNG) pricing is highly complex, due to international price changes, varying cost of intermediary logistic services etc. Thus, secret comparables obtained from corporates are usually far from accurate and hence should not be applied for determination of arm's length price of LNG. Allowing use of secret comparables for non-commodities leads to a high number of disputes and unwarranted litigation. Arms-length price for LNG needs to account for functional differences. Developed countries, such as the US & UK have an official policy of not using secret comparables for any Arm's Length Principle (ALP) evaluation. In Australia and Netherlands, under specific judicial pronouncements, secret comparables are not allowed. It is recommended that secret comparison analysis should not be made applicable for non-commodities like LNG.

3.11.25. Presumptive Taxation Regime – Section 44BB

A. Application of Section 44BB where Section 44DA applies

Under section 44BB of the Act, non-resident services providers to extraction or production of oil sector have an option to be taxed at a gross rate of 10 percent of receipts on presumptive basis. Amendment was introduced in 2010, wherein provisions of section 44BB will not be applicable where provision of section 44DA of the Act is applicable. This has resulted in ambiguity regarding applicability of provisions of section 44BB to non-residents providing services that are technical in nature to an Indian concern.

This has challenged the settled tax position and resulted in tax litigation. Tax authorities have applied this amendment across all services in connection with exploration/production of oil & gas, by arguing that such services involve usage of technical knowledge and hence provisions of section 44BB of the Act are not applicable. The Supreme Court in the case of Oil and Natural Gas Corporation Limited vs. CIT in Civil Appeal No. 731 of 2007 (SC) has held that any services rendered which is directly associated or inextricably connected with prospecting, extraction or production of mineral oil should be covered within the provisions of section 44BB of the Act. It is therefore suggested that appropriate directions be issued by the Government for must adherence by the field officers to the effect that presumptive taxation regime under section 44BB of the Act is applicable to non-residents for services

rendered in connection with prospecting for, or extraction or production of mineral oils even if the same are technical in nature.

B. Statutory Taxes not to form part of Gross Receipts

Section 44BB of the Act provide for taxation of non-residents on a presumptive basis. This section deems a specified percentage of the amounts received by the non-residents for the activities covered by provisions of section 44BB of the Act. In the past there has been considerable litigation on whether Government dues, such as service tax, recovered by the non-residents from the Indian parties would constitute part of gross receipts as these statutory dues are to be paid over by the non-resident taxpayers to the Government, there is no income element therein.

In view of the above, section 44BB of the Act should be amended to provide that statutory taxes and dues recovered by the non-resident service provider from the Indian residents would not form part of gross receipts for computing deemed income under the Section. This will be fair and will eliminate unnecessary litigation on the issue.

C. Applicability of beneficial tax regime under section 44BB be made available to sub-contractors

Under section 44BB of the Act, non-resident services providers to extraction or production of oil sector have an option to be taxed at a gross rate of 10 percent of receipts on presumptive basis. There is no express requirement that the person providing services should have direct contractual relationship with the person engaged in prospecting, extraction and production of oil. The intention behind beneficial tax regime is to promote Oil and Gas industry by encouraging foreign companies providing services in connection with Oil exploration activities. The essence of the transaction remains unaltered even if these foreign companies are engaged by Indian Contractors for provision of offshore services and not directly by the oil production/processing industry. It is therefore suggested that suitable amendment be made in section 44BB of the Act to provide clearly the applicability of the beneficial tax regime under section 44BB of the Act to sub-contractors.

3.11.26. Remove Ceiling on Profits for Site Restoration Fund (SRF) Contribution

Abandonment and site restoration of oil and gas installations are significant part of the project life cycle in the E&P sector. This phase involves huge capital outlay and has considerable environmental implications. Section 33ABA of the Act provides for tax deduction on contribution to the Site Restoration Fund (SRF) subject to a ceiling of 20% of the profits from the business. This ceiling could result in a situation where the assesse is unable to claim full deduction for the amount deposited in the SRF in the absence of sufficient profits. It is, therefore, recommended that the deduction should be based on full contribution without any ceiling on profits.

INFORMATION TECHNOLOGY (IT) AND TELECOMMUNICATIONS

3.12.1. Clarity on utilization of SEZ Re-investment Reserve Account – Section 10AA

The tax holiday under section 10AA of the Act in the years 11 to 15 of operation of SEZ is available only on creation and utilization of the SEZ re-investment reserve. The potential

issues the tax payer is facing in interpreting the reserve related provisions are discussed as under:

- There is an ambiguity as to whether the SEZ reserve can be utilized in the year of creation itself.
- Further, there is also an ambiguity on whether the SEZ reserve is required to be utilized for acquiring plant and machinery within the same SEZ unit or can be utilised for any other SEZ unit/ other unit.

It is suggested that appropriate clarification be provided in regard to the above issues for claiming deduction under section 10AA of the Act for the year 11 to year 15.

3.12.2. Clarity on Tax Treatment of Spectrum Payments

Telecom companies considers spectrum as an intangible asset and capitalise the cost incurred for acquisition of the spectrum to the block of assets. The companies have been claiming tax depreciation under section 32 of the Act. However, the tax authorities are largely taking a position that spectrum payments are eligible for amortization under section 35ABB of the Act which provides for amortization of license fee. The Finance Act 2017, introduced Section 35ABA with effect from April 1, 2017 (AY 2017-18), which provides for amortization of spectrum payments. This is in line with the industry's position that spectrum payments cannot be amortized under section 35ABB (which covers only license to operate telecommunication services).

There is ambiguity prevailing with regard to the tax treatment of spectrum acquired and put to use prior to AY 2017-08 since provisions of section 35ABA are applicable from AY 2017-2018. It is accordingly suggested that it may be clarified that the provision of section 35ABB and Section 35ABA shall not apply to spectrums acquired upto 31 March 2016. It should be further clarified that the spectrum acquired upto 31 March 2016 is in the nature of an intangible asset on which tax depreciation can be availed under section 32 of the Act.

3.12.3. Amendment of definition of 'industrial undertaking' to include telecom infrastructure service providers

Under the existing provisions contained in section 72A of the Act, the benefit of carry forward of losses and unabsorbed depreciation is allowed in cases of amalgamation of a company owning an industrial undertaking or a ship, with another company. Industrial undertaking is defined to mean any undertaking which is engaged in the manufacture or processing of goods or computer software, the business of generation or distribution of electricity or any other form of power, the business of providing telecommunication services, whether basic or cellular, including radio paging, domestic satellite service, network of trunking, broadband network and internet services, mining or the construction of ships, aircrafts and railway systems. Definition of Industrial Undertaking for the purpose of section 72A of the Act does not include telecom infrastructure companies, to allow accumulated losses and unabsorbed depreciation in the hands of the tower infrastructure companies. Unprecedented increase in adoption of digital services such as payments, e-

governance and entertainment will necessitate further investments in the telecom infrastructure sector.

To encourage rapid consolidation and growth in an important infrastructural area the benefit under section 72A of the Act should be extended to include tower infrastructure companies.

3.12.4. TDS on prepaid distributor margins/discounts from telecom operators

It is a practice in the telecom industry to enter into an arrangement with the pre-paid distributors on "Principal to Principal" basis such that all material is supplied at a discount to the MRP and the distributor can, in turn, sell at any price up to the MSP (max selling price) of the product. The risk of any losses is not borne by the telecom operator but by the distributor. There has been continuous litigation on whether the relationship between the telecom companies and distributors is on "Principal to Principal" or "Principal to Agent" basis. TDS is applicable only if the relationship is of principal to agent basis else not. It is strongly believed that issuance of a clarification that such discounts does not fall within the ambit of TDS provisions is warranted. Alternatively, it is suggested that the Government should introduce the TDS rate of 1% on such payments, 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.

3.12.5. TDS on International Interconnect Charge (IUC) and Bandwidth Charges paid to foreign telecom operators

The Finance Act 2012 brought in a retrospective amendment to the definition of the term 'Royalty' by introducing Explanation 6 to Sec 9(1)(vi) of the Act. As per the amendment, the term 'process' used in the existing definition of 'Royalty' has been elaborated to include transmission by satellite, cable, optical fiber or by any other similar technology, whether or not such process is secret. The amendment made in the definition of 'Royalty' under the Act vide Finance Act 2012 with retrospective effect cannot override the scope of 'Royalty' provided under the Double Taxation Avoidance Agreements (DTAA/tax treaties) entered by India with other countries. In absence of definition of the term process in most of the tax treaties, the tax officers have disallowed genuine business expenditure incurred by Indian telecom companies towards bandwidth, satellite, roaming and interconnect charges (IUC) by invoking section 40(a)(i) of the Act. It is suggested that a clarification be issued that retrospective amendment in the definition of 'Royalty' would not have any bearing on the interpretation of the term in tax treaty and the enlarged scope of definition in the Act would not be imported in the tax treaty. It is further recommended that definition of royalty in the Act should be amended to exclude Interconnect Charge (IUC) and Bandwidth Charges being payment for mere standard services.

INFRASTRUCTURE

GST

3.13.1. Review GST rates for all infrastructure related works contract

The rate of GST on specified works contract pertaining to roads, bridge, tunnel or terminal for road transportation for use by general public and specified schemes by government has

been reduced from 18% to 12% vide notification no. 20/2017- Central tax (rate) dated August 22, 2017. The notification also covers original works pertaining to railways and specified housing scheme of government. However, the rate for works contract pertaining to ports, airports, metro, mono rails etc. remains 18%. It is suggested that rate of GST on works contract service provided to both private and public/ government authorities relating to all infrastructure projects, such as ports, airports, metros, mono rails, power plants, oil & gas refineries etc. should also be reduced to 12%.

DIRECT TAX

3.13.2. Request for Discounted Cash Flow Method to be prescribed for valuation in case of infrastructure investments

In case of infrastructure assets, the ability of the asset to generate future cash flows is the key determinant to valuation. Hence for an investor, the key factor in arriving at the fair market value of these assets would be the underlying ability of the asset to generate cash flows and not the value at which the existing owner has acquired or built it and carried forward in books of accounts. Considering the foregoing, Discounted Cash Flow (DCF) methodology is therefore an appropriate valuation approach for investors in infrastructure assets. Reference to book value in the hands of existing owner may not be relevant and may lead to frustration in the process of attracting new capital. The Central Board of Direct Taxes (CBDT) has published rules for Sections 50CA and 56(2)(x) of the Income Tax Act, to substitute existing rules as set out in Rule 11UA of the Income Tax Rules, 1962 for computing Fair Market value of unquoted equity shares. Application of Book Value as the Fair Market Value (except in case of certain assets) leads to severe tax consequences if the Fair Market Value based on DCF approach is lower. On one hand, the buyer has to pay tax on the difference between book value and purchase consideration, when in fact no gain/benefit has been received by the buyer. On the other hand, the seller has to pay capital gains on the difference between FMV and the sale consideration, when in fact the seller is actually incurring a loss. Consequently, many infrastructure sale transactions would be rendered unviable, both from a sellers' and buyer's perspective. There could be situations where buyer and seller end up paying taxes more than the actual sale consideration, which is grossly unjust and would deter the business sentiment particularly when the Government is trying to access fresh capital into the sector through InvITs and REITS and also to address the NPA issue in the banking system and to revive the ailing infrastructure sector with fresh capital.

The key is therefore to differentiate private transactions having opaque price discovery processes which have been structured with the purpose of tax avoidance from transactions where the price discovery has been through a transparent and arm's length process in the public domain. The asset value arrived on the basis of internationally accepted valuation methodology like DCF and undertaken through a transparent process with sufficient regulatory oversight needs to be considered as the Fair Market Value.

It is suggested that the Rules may appropriately be amended to prescribe DCF method of computing Fair Market Value in case of transfer of infrastructure assets where a carve out can be made under the provisions discussed above for transfer of assets effected under the

InvIT framework as approved by SEBI, and schemes to resolve stressed assets administered by RBI and NCLT.

MANUFACTURING – CAPITAL GOODS, ELECTRONICS AND CONSUMER DURABLES

CAPITAL GOODS

3.14.1. Rationalisation of Inverted Duty Structure in case of Capital Goods

An inverted duty structure refers to a situation where manufacturers have to pay a higher duty on raw material while the resultant finished product attracts lower duty. Some of the instances leading to inverted duty structure in case of capital goods are listed below for the consideration of the Government:-

(a) Import duty on boilers is 1.56% and its parts are subject to zero custom duty whereas large number of components and steel plates required for manufacture of boilers is subject to basic customs duty of 7.5% to 10%. This anomaly needs to be removed by appropriate duty rationalization. The details of duties presently levied are given below:-

HS Code	Description	Rate of Basic Customs Duty
84021100	Watertube boilers with a steam production exceeding 45t per hour - S.No. 631 of Customs notification 152/2009 read with 60/2015 when imported from Korea	Zero
84029020	Parts of water tube boilers - S.No. 632 of Customs notification 152/2009 read with 60/2015 when imported from Korea	Zero
RAW MATERIALS AND COMPONENTS		
84145990	Air or vacuum pumps	7.5%
84818030	Industrial valves (excluding pressure-reducing valves, and thermostatically controlled valves)	7.5%
73069090	Other tubes, pipes and hollow profile of iron or steel	10%
84219900	Centrifuges including centrifugal dryers	7.5%
85042100	Electrical transformers, static converters and inductors, having a power handling capacity not	7.5%

	exceeding 650 KVA	
84819090	Taps, cocks, valves and similar appliances for pipes	7.5%
85372000	Boards, panels, consoles, desks, cabinets and other bases for electric control or the distribution of electricity, For a voltage exceeding 1,000 V	7.5%
85446090	Insulated wire cable	7.5%
85371000	Boards, panels, consoles, desks, cabinets and other bases for electric control or the distribution of electricity, For a voltage not exceeding 1,000 V	7.5%
85013119	Electric motors and generators(excluding generating sets)	7.5%
84139190	Pumps for liquids	7.5%
90328990	Automatic regulating or controlling instruments	7.5%
73079990	Tubes or pipe fittings of iron & steel	10%

(b) Import duty on mechanical presses (machine tools) is zero whereas large number of components and steel plates used for manufacture of these capital goods is subject to customs duty of 7.5% to 12.5%. This again is a case for duty rationalisation. The details of duties presently levied on inputs are given below:-

HS Code	Description	Rate of Basic Customs Duty
84629099	Mechanical Presses (Machine Tools) Customs notification No.152/2009 S.No.747	Zero

RAW MATERIALS AND COMPONENTS

72085110	Steel plates	12.50%
84669400	parts of machine tools	7.5%

84836090	Hydraulic progressive control unit	7.5%
84836090	Hydraulic combined clutch and brake	7.5%
84814000	Press Safety Valves	7.5%
72192112	Stainless steel plates	7.5%
90318000	Linear Displacement Transducer	7.5%
84149090	Double Discharge Van Pump	10%

(c) Import duty on pressure vessels is zero whereas large number of components and steel plates used for manufacture of these capital goods is subject to customs duty of 7.5% to 12.5%. As this is the case for duty inversion, appropriate duty rationalisation needs to be carried out. The details of duties presently levied are given below:-

HS Code	**Description**	**Rate of Basic Customs Duty**
84198910	Pressure Vessels Customs notification No.151/2009 S.No.34	Zero

RAW MATERIALS AND COMPONENTS

72085110	Steel plates	12.50%
73269099	Forged components	10%
72254012	Alloy steel plates	10%
83112000	Welding wire and electrodes	10%
38101010	Welding flux	7.5%

72192112	Stainless steel plates	10%
73043919	Carbon steel pipes	10%
73045910	Alloy steel pipes	10%
73044900	Stainless steel pipes	10%
73079990	Fittings	10%

ELECTRONICS

While the Indian electronics sector has been witnessing a consistent growth in terms of market size, India lags behind in electronics hardware manufacturing capabilities due to innumerable challenges including high cost of power and finance, high transactional costs, prevalent tax structure and poor base of supply chain. Some of the issues and recommendations in this regard for the consideration of the Government are given below:-

3.14.2. Incentivise Design-led Growth Investment in R&D and IPR

Electronics manufacturing in India is confined to low end value chain. There is need to transition to Design in India and IP creation. Currently, private sector R&D does not get Government funding unless it ties up with Government R&D organizations. India has a promising hardware engineering talent and vibrant design competencies; hence Design in India can lead to Make in India. There are various design elements such as the whole fabrication, mechanical design, the PCB (printed circuit board) layout, component selection, RF testing that can be done in India. It is suggested that suitable incentives may be introduced by the Government to encourage Design in India to achieve Make in India with increased focus on R&D and IPR. Design in India will ultimately lead to job creation, generating intellectual property, address huge domestic demand and export opportunities, creation of local component ecosystem, and manufacturing of world class products in India.

3.14.3. Incentivise manufacturing by providing throughput based incentive

All incentives available to manufacturing are capex based incentive. It is recommended that the Government may consider providing throughput based incentive (on what we manufacture) both for domestic and export for a timeframe of three to four years. One way to provide this incentive is through the provision of production subsidy which has been introduced under the MSIPS Scheme vide notification of 3rd August 2015 (which includes high value added items such as semiconductor wafering, logic microprocessors, ICs and added new components such as PCB, discrete semiconductors fab, Power Semiconductors Fab and ATMP etc.).This provides for a 10% Production Subsidy on the value addition by the manufacturing unit. Thus, higher the value addition, higher the subsidy and vice versa. It is recommended that production subsidy be extended to include all components & raw materials which are covered under Information Technology Agreement 1 and are subject to Zero Customs Duty.

3.14.4. Increase Basic Customs Duty on Select Products

The BCD on import of select non-ITA goods be raised to a permissible limit in order to discourage the traders from importing such goods into India and selling the final product with mere screw driver assembly technology. These products/Finished Goods should however be decided with Industry consultation. The high technology and low volume products should not be considered for any such BCD raise and only the products which are in voluminous in nature and have developed local indigenisation capability or being manufactured in the country should come under BCD raise. The discrete components however may be exempted from levy of BCD when imported into India for manufacture of these products/finished goods. However, the Populated Printed Circuit Boards be brought under the levy of Basic Customs Duty as it will give encouragement to local value addition.

3.14.5. Encourage domestic manufacturing of Printed Circuit Board Assembly ('PCBA')

PCB is considered to be most important component of any Electronics/electronic product. India has potential to populate PCB in India. There are more than 500 sophisticated Surface-mount technology (SMT) lines that are available which can take up manufacturing of populated PCBs immediately. In absence of PCB manufacturing, many of the companies have curbed their manufacturing operations and switched to trading and some of them get their products manufactured through overseas EMS providers in Taiwan/China. These companies can entice their EMS providers, who have already shown inclination to relocate to India if the benefits being made available for domestic manufacturing on populated PCBs along with existing demand for their products. It is accordingly recommended that PCB assemblies of non-ITA-1 items should be subjected to minimum customs duty. This would ensure that the basic customs duty becomes a cost in the import of PCBA which would create duty differentiation between imports and domestic manufacture.

3.14.6. Provide Clarity on rate of GST on toner cartridges

There is no clarity on the applicability of rate of GST on toner cartridges. It is recommended that suitable clarity be provided on the rate of GST applicable to toner cartridges to avoid any litigation on this account in future.

3.14.7. Provide Clarity on availability of input tax credit on inputs used for in-warranty/AMC supplies

A warranty is a written guarantee for a product and it declares the responsibility of the maker to repair or replace any defective products or parts. While the rectification is done on a free of cost basis, the cost of rectifying the defect is included in the original price at which the goods are supplied. Further, in case of annual maintenance contracts (AMC) supplies, the cost for providing the repair is collected at the time of entering into the AMC contract and the goods are supplied free of cost subsequently when the time arises for repair of goods. Under the GST regime, there is ambiguity as to whether the supplier would be eligible to claim input on procurement of parts which shall be used for warranty replacement and AMC. It is recommended that appropriate clarity be provided that ITC shall be allowed on parts used for warranty replacement or in case of AMCs.

3.14.8. Provide clarity on refund of input tax credit in the case of inverted duty structure due to input services

As per first proviso to section 54(3) of the CGST Act, 2017, refund of unutilized input tax credit is allowed in the following two instances:-

"(i) zero rated supplies made without payment of tax;

(ii) where the credit has accumulated on account of rate of tax on inputs being higher than the rate of tax on output supplies (other than nil rated or fully exempt supplies), except supplies of goods or services or both as may be notified by the Government on the recommendations of the Council."

As per the above provision one of the cases where refund of input tax credit is allowed is when unutilized credit is on account of rate of GST paid on inputs being higher than the rate of GST on outward supplies made by the supplier. However, there is ambiguity regarding refund of input tax credit in case where the inverted duty structure arises as a result of rate of tax on input services being at a higher rate in comparison to the outward supplies. It is requested that appropriate amendment be made in the GST law to provide for allowability of refund in case of inverted duty structure arising on account of input services. This would provide much needed clarity on this aspect.

3.14.9. Reduce customs duty on compressors, motors, electronic components

There are components like high efficiency compressors and motors, Electronic components, vacuum insulation panels (required for meeting the higher BEE energy regime) which either do not have domestic manufacturers or there are severe capacity and competition constraints, accordingly the peak duty structure of 7.5% should be reduced. This will help the energy regime to deliver better products to the customer at reasonable prices.

3.14.10. Reduce rate of GST on Mixer Grinder

Electro mechanical domestic appliances like Mixer Grinder falls under chapter heading 8509. The relevant entry reads as follows "Electro-mechanical domestic appliances, with self-contained electric motor, other than vacuum cleaners of heading 8508 [other than wet grinder consisting of stone as a grinder]".

Mixer Grinder is a product commonly used in almost every household. In modern day cooking, no food preparation can be complete without using a mixer grinder. Thus, it has become an apparatus of necessity in very common man's household.

Taxing mixer grinder @ 28% would increase the tax burden on the said product thus, making it unaffordable. Therefore, it is recommended that the rate on Mixer Grinder should be reduced from 28% to 12%. Further, recently, the GST rate on wet grinder consisting of stone as grinder has been reduced to 12% from 28%. However, Mixer Grinder continues to be taxable at 28%. Accordingly, in order to bring parity, it is requested that the tax rates on grinder as a whole should be lowered to 12%.

CONSUMER DURABLES

3.14.11. Reduce GST Rates

The consumer durables has been placed in the same bracket of tax as applicable to sin goods. These goods are subject to the highest rate of GST @ 28%. It is submitted that consumer durables are essentials and cannot be considered as luxury especially items such refrigerators and washing machines in today's era. It is emphasized that the rate of GST on consumer durables should be reviewed and reduced by the Government at the earliest.

MEDIA AND ENTERTAINMENT

GST

3.15.1. State Government Entertainment Tax – Exemption of Tax (Grandfathering and upcoming properties) and grant of service charge to Regional Film Producers and Cinema Exhibitors

Many state governments including the State of Maharashtra, West Bengal, Orissa, Rajasthan, UP & Punjab etc. had announced the Entertainment duty exemption schemes for new facilities as well as in respect of renovation to install latest equipment like projection, sound system and comfortable chairs etc. The tax exemptions have been granted from 5 to 7 years and many of them are under the grant period. If this tax exemption is removed then the exhibitors who have invested huge amount for renovation by borrowing loans from financial institutions may not be able to repay the loans and also to recover their cost. It is requested that such cinema owners be allowed refund in a proper time frame under the GST regime in respect of the exemption committed under the erstwhile regime. Additionally, the commitment made by Government prior to GST regime, should be honoured on the priority. The refund granted should be based on the original commitment by extending the tenure of the expired period and not be limited to the SGST portion only.

The Regional Films in many states are granted total exemption from the Entertainment duty and subsidies are granted for the production of the films. This has also helped producers to survive in difficult conditions.

For the modernisation and maintenance of the cinemas the State Governments have permitted the cinema exhibitors to retain part amount of the admission rates as Service Charge and no entertainment duty is charged on this retention. If this is removed no cinema will be able to survive.

This is a very big relief to especially the Single Screen Exhibition trade to maintain and upkeep their cinemas and compete with Multiplexes.

It is requested that these important exemptions/service charges in the state entertainment regime be further continued in the GST regime also.

3.15.2. Subsume Local Body Entertainment Tax in GST

Various states like Tamil Nadu, Gujarat, Rajasthan, Maharashtra, Haryana and Chandigarh have already authorised their local bodies to levy entertainment tax on entertainment including Cinema Exhibition and many other states are contemplating doing so. Tamil Nadu

has already implemented LBET @ 8% on Tamil Movies, 15% on Hindi Movies and 20% on English Movies. The levy of local body entertainment tax defeats the basic purpose of implementing GST.

In addition, imposition of such a levy would entail compliance and enforcement challenges. It is accordingly suggested that this local body tax be subsumed in SGST and suitable allocation to the local body be made to compensate them for their shortfall, if any.

DIRECT TAX

3.15.3. Deduction for cost of production/acquisition for film producers/distributors – Rules 9A and 9B

Rules 9A and 9B of the Rules deal with deduction of expenditure for production of films. These Rules refer to exhibition of films on a commercial basis and are silent on the modes of such exhibition. It is suggested that for determination of "distribution of film on commercial basis" any of revenue streams such as music, digital, satellite should be considered and further appropriate clarity be provided by the Government, with the growth of digital business and advent of new revenue streams. It is further suggested that the entire cost of production should be allowed in the year of film release irrespective of the date of release.

3.15.4. Clarity on Royalty - Film distribution rights – Section 9(1)(vi)

There is an ongoing litigation on whether transfer of film distribution rights would constitute royalty. The definition of royalty under the domestic tax laws includes consideration for transfer of all or any rights (including grant of license) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting, but not including consideration for the sale, distribution or exhibition of cinematographic films. On a reading of the above definition, one would observe that consideration for "sale, distribution or exhibition" of "cinematographic films" is excluded from the royalty definition. The key issues are as to what constituents a "cinematographic film", and second, whether license of distribution rights amounts to "sale, distribution or exhibition" for the purpose of the above exclusion. It is requested that appropriate clarification in this regard may be provided to put an end to litigation on this issue.

MSMEs

3.16.1. Facilitate level playing field under GST Regime for SITP Parks in line with SIDCs

The Textile Parks developed/to be developed under the Scheme of Integrated Textile Parks (SITP) Scheme are promoted by Ministry of Textiles, Government of India. The Textile Parks developed/to be developed under SITP Scheme and Industrial Parks developed/to be developed by the State Industrial Development Corporation / Undertakings (SIDC) are on the same business model.

The Government has levied GST on 'Real estate services' @ 18% under chapter heading 9972 vide serial number 16 of the Notification No. 11/2017 – Central Tax (Rate) dated 28th, June, 2017 wherein the upfront amount taken from members for development of infrastructure of parks shall be charged to GST @ 18%. However the Government had given

exemption from the whole of GST leviable on "One time upfront amount (called as premium, salami, cost, price, development charges or by any other name) leviable in respect of the service, by way of granting long term (thirty years, or more) lease of industrial plots by the State Government Industrial Corporation (SIDCs) to industrial units under chapter heading 9972 vide serial number 41 of the Notification No. 12/2017 – Central Tax (Rate) dated 28th June, 2017. It was further decided by the GST Council in the October 6th meeting that "Exemption will be provided to upfront amount payable in respect of granting long term lease of thirty years, or more of industrial plots or plots for development of infrastructure for financial business, provided by the State Government Industrial Development Corporations/Undertakings or any other entity having 50% or more ownership of Central Government, State Government, Union Territory to (a) industrial units or (b) developers in any industrial or financial business area".

It may be noted that under SITP the park ownership does not belong to the Central Government, State Government or Union Territory but 40% of the project cost (subject to ceilings) is funded by the Government in the form of either equity or grant to establish the Parks. As per the scheme the funding by the Government in the textile park would be generally in the form of grant and even where it is in the form of equity, the combined equity of Government of India, State Government/ SIDC (if any) cannot exceed 49% in the SITP. Accordingly, the benefit of the aforesaid notification will not be available to textile parks established under SITP funded by the Government in the form of grant or through equity.

The Government attaches highest priority to the sustainability of parks established under SITP, for which achieving financial viability is the key. It is recommended that a similar notification to provide exemption from GST on the cost of infrastructure recovered in the form of contribution towards infrastructure/development charges/lease premium from members/ industries at the time of lease with respect to SITP". The exemption from GST provided to SIDCs may be extended to SITP with retrospective effect to provide them a level playing field with SIDCs.

The exemption given to SIDCs and not to SITPs is not providing level playing field to SITPs and would lead to injustice for MSMEs.

3.16.2. Provide Interest Subvention Scheme for MSMEs

Banks are generally charging higher interest from MSMEs. It is recommended that scheme of interest subvention now known as Interest Equalisation Scheme should be provided by Government to MSMEs in general as currently provided in case of Pre & Post Shipment Rupee Export Credit only. The reduced rate of interest would help the units which are generally driven by individual or small entrepreneurs. This would encourage the growth of the entire MSME sector.

NON FERROUS METALS

I – COPPER

3.17.1. Exemption from levy of Import Duty on Copper Concentrate

Copper is a critical input for various industries, including infrastructure indicators. The critical raw material for this industry, i.e. copper concentrate, is available very scarcely in India, making it imperative for the country to import either refined copper or copper concentrate. Given the structural constraint of non-availability of copper concentrate, Indian producers set up custom copper smelters (similar to the business models of China, Japan and Korea) based on imported concentrate. Nearly 90% of the requirement for copper concentrates is met through imports.

Hence, it is recommended that copper concentrate be exempted from basic customs duty to ensure domestic availability of copper concentrates. Also, with finished copper products getting imported at appx NIL import duty under FTAs, there is a case of inverted duty structure that needs to be corrected.

3.17.2. Reduce Import Duty on Raw materials used in products of Copper

Due to FTA with ASEAN, finished and semi-finished products of copper and other alloys are imported into India at nil rates whereas raw material is chargeable at 5%. Copper Cathodes (HS 74031100), Copper Rods (HS 74031200), Brass Scrap (HS 74040022), Zinc Ingots (HS 79011100, 79011200), Copper Blisters (HS 74020010), Copper Anode (HS 74020090) are subjected to an import duty of 5%. It is suggested that import duty on all above mentioned raw materials should be removed.

It is also recommended that the export incentives in respect of Copper Cathodes and Copper Rods should be reinstated.

3.17.3. Tariff Classification under GST

On perusal of the Tariff Classification under GST for HSN Code 7410 it has been observed that the thickness range for Copper Foils (7410) has been not been mentioned. The Tariff Classification under Customs for HSN 7410 specifies “COPPER FOIL (WHETHER OR NOT PRINTED OR BACKED WITH PAPER, PAPERBOARD, PLASTICS OR SIMILAR BACKING MATERIALS) OF A THICKNESS (EXCLUDING ANY BACKING) NOT EXCEEDING 0.12.5 MM”.

It is requested that Tariff Classification under GST regime for HSN Code 7410 be aligned with Tariff Classification under Customs in respect of HSN Code 7410 to avoid classification disputes on this matter in future.

II – ALUMINIUM

3.17.4. Removal of Import Duty on Alumina

In India, Alumina is a primary raw material for Aluminium production and constitutes ~40-45% of cost of production of Aluminium metal. The Aluminium producers are importing Alumina to meet domestic industry requirement as majority of bauxite ore deposits are still unexplored.

In 2016-17, India imported 9.21 lakh tonnes Alumina (31% increase over FY15- 7.02 lakh tonnes). The import of alumina is set to increase with the operationalization of upcoming expansion smelter capacities.

The cost of production of aluminium metal in India has increased considerably over past 3-4 years due to increased cost of raw materials, clean environment cess on coal- (Rs. 400/MT) (replaced with GST Compensation Cess of equivalent value under GST regime and Renewable Power Obligation (RPO) and high logistic costs.

The high import duties on raw materials has a huge disadvantage for domestic aluminium producers which are dependent on imported raw materials, rendering Indian finished goods costlier and uncompetitive in international markets, and discourages domestic value addition within the country.

Hence, FICCI recommends for removal of import duty on alumina (28182010) from 5% to NIL to encourage domestic value addition within the country and thereby increasing exports of Aluminium and its finished products.

3.17.5. Reducing Import Duty on Aluminium Fluoride

India is net importer of Aluminium fluoride (AlF3). Aluminium industry is importing 100% of its requirement of AlF3. Contribution of Aluminium fluoride in cost of production of aluminium with metal is around 1.5%. The demand for AlF3 will increase the operationalization of expansion projects. Duty correction on AlF3 will not have any impact on any other industry. Hence, it is recommended to reduce import duty on Aluminium Fluoride (28261200) from 7.5% to 2.5%.

3.17.6. Reducing Import Duty on Coal Tar Pitch to 2.5%

Coal Tar (CT) Pitch is a crucial raw material for aluminium to be used as binding material for manufacturing anodes for the electrolysis process with the aluminium industry using a substantial quantity of total production/imports of CT Pitch. Its contribution in the total cost of production of aluminium is around 3.5-4%. It is suggested to reduce import duty on CT Pitch (27081010) from 5% to 2.5%.

3.17.7. Reducing Import Duty on Caustic Soda to 2.5%

Caustic soda (28151200) is one of the major raw materials for the production of alumina, which is an intermediate product for production of aluminium metal from aluminium ore (bauxite). Caustic soda contributes around 13% in cost of production of alumina. One of the largest bulk consumers for the commodity, the aluminium industry contributes around 14% of total Indian demand for caustic soda. Aluminium industry imports almost 100% of its requirement of caustic soda contributing around 75% to the total imports of caustic soda. It is recommended to reduce import duty on Caustic Soda (28151200) from 7.5% to 2.5%.

3.17.8. Increase in Basic Customs Duty on aluminium and its products

Indian Aluminium Industry has seen a huge surge in imports in recent years primarily from China and Middle East which have surplus aluminium capacity and their Aluminium Industry is supported by government in form of concessions/subsidies with cheap power tariff, low

cost gas allocations, tax benefits, and VAT rebates on exports bringing down the production costs. India's aluminium domestic industry capacity is capable of meeting 125% of the domestic consumption, but it is only able to supply 47% of domestic market demand and 53% of India's aluminium demand is being met through imports.

In FY17 India's aluminium imports increased by 5% to 1751 kt over FY16 with 1670 kt, while domestic sales declined by 2% despite increasing domestic aluminium consumption.

The high imports have resulted in declining domestic market share of primary producers (declined from 60% in FY11 to 47% in FY17) and underutilized capacities rendering huge financial losses.

Therefore, it is recommended to increase custom duty for all aluminium products for HS Code 7601, 7603 to 7607 from 7.5% to 10% and for HS Code 7608 to 7616 from 10% to 12.5% which will restrict imports and increase domestic capacity utilization thereby generating employment and boosting government's visionary Make in India initiative.

3.17.9. Customs duty on Aluminium Scrap to be at par with the duty on the metal products

For all base metals other than Aluminium, import duty on scrap in India is the same as the duty on the metal. It is only in case of Aluminium that the duty on scrap is 2.5%, while duty on aluminium products is at 7.5%. In most of the Aluminium downstream products, scrap and primary aluminium can be used almost interchangeably. The differential duty structure seems to be, therefore, leading to a substitution of primary aluminium by scrap – reflected in a sharp rise in imports of scrap (CH 7602). Scrap imports are causing an immense harm to the Indian aluminium industry due to market diversion.

It is recommended increasing import duty on Aluminium scrap (HS Code 7602) at par with primary metal, as in line with other non-ferrous metals like copper, zinc, lead, nickel, tin etc. have same custom duty for scrap and primary metal.

3.17.10. Inclusion of Aluminium in Interest Equalization Scheme

In order to encourage exports, Government of India has introduced the Interest Equalization Scheme, however, Aluminium is one of the major export items which is not included in the list. It is therefore requested that Aluminium (Chapter 76) be included in the Interest Equalization Scheme.

3.17.11. Increasing Export Duty on Bauxite from 15% to 20%

India is well placed in terms of raw material availability for aluminium production and has 5th largest bauxite reserves in the world (estimated to be over 3.7 billion tonnes).

Since no new major bauxite mines could be started in the last 20 years, Alumina refineries in India are finding it difficult to source indigenous bauxite and are forced to import. On the other hand merchant miners are exporting huge quantities of bauxite.

Currently Indian Alumina refinery capacity is 6.28 mtpa and bauxite requirement is 18.8 mtpa. With upcoming expansion projects the total alumina refining capacity will increase to 12.8 mtpa having bauxite requirement of 38.3 mtpa.

In FY 17, India exported 1830 kt bauxite (both calcined and not calcined) and at the same imported 1716 kt bauxite for meeting domestic industry requirements. Majority of bauxite from India is exported to China, thereby supporting Chinese value addition through their aluminium industry which exports finished Aluminium products back to India.

To ensure domestic value addition within India, export of bauxite must be discouraged. It is therefore suggested to increase export duty on bauxite from 15% to 20%. This shall boost exports of finished aluminium products and generate employment opportunities in the downstream sectors.

3.17.12. Remove GST Compensation Cess on Coal

The Clean Environment Cess on coal (Rs. 400/MT) has been replaced with GST Compensation cess of equivalent value under GST regime. This cess was introduced as clean energy cess in 2010 with levy of Rs. 50/MT on coal and there has been repeated hike in this cess over the last few years from Rs. 50/MT to Rs. 100 MT in 2014-2015, to Rs. 200/MT in 2015-2016 which was further increased to Rs. 400/MT through Union Budget 2016-2017. The increase in cess had an adverse impact on the power intensive industries and thus rendering industry operations economically unviable, operating at reduced capacities with risk of plant closure. It is emphasized that levy of GST Compensation cess on coal needs to be reviewed. The removal or at least reduction in this cess will provide big support to power intensive industries and will help them retain competitiveness.

III- LEAD

3.17.13. Increase in Basic Custom Duty on Lead Ingots (HS Code 780110) & Lead Scrap (HS Code 780200)

Indian primary Lead industry is going through a tough time with input costs increasing year on year due to higher exploration costs, mining expenses, lower concentrate treatment charges, coupled with the increase royalty charges, and falling concentrate grades. Thus smelting of lead metal is becoming a costly affair with revenue generation capability being limited as pricing is based on an index (LME). Lead producers are 'price takers' and do not have control on fixing of prices.

While developed countries in the western world have very stringent norms for import and recycling of Lead scrap and have recently announced cancellation of licenses in unscrupulous recycling of imported lead scrap, in India, the duty on lead battery scrap is zero which leads to increase in imports.

Considering the sharp increase of Lead imports from Financial Year 2011 to Financial Year 2017 (48% increase) and due to various challenges faced by the lead industry including increase in input costs, it is requested that the basic custom duty on Lead Ingots (HS 780110) & lead scrap (HS 780200) be increased from 5% to 7.5%.

3.17.14. Reduce Basic Custom Duty on Lead Concentrate (HS Code 260700)

Limited availability of ore in the country leads to shortage of Lead ore and concentrates and hence further leading to production capacities lying idle. High import duties on concentrate

make production of Lead ingots costlier and face stiff competition from international players both in the domestic as well as international market.

Although customs duty on lead metal is pegged at 5% since January 2007, in view of the multiple preferential trade agreements, the effective duty on lead metal is now Nil, especially when imported from South Korea and marginal when imported from Japan. At the same time, the customs duty on raw material (Lead con) is 2.5%, leading to a clear inverted duty structure.

Favourite conditions around nil basic duty on raw material and conducive tax and regulatory environment for domestic industry, would ensure that the Industrial capacities for Lead operate at 100% capacity utilization rates. It is accordingly recommended that basic customs duty on Lead Concentrate (HS Code 260700), the basic raw material for producing Lead Ingots be reduced from existing 2.5% to Nil.

IV – ZINC

3.17.15. Increase in Basic Customs Duty on Zinc Ingots (HS 790111, 790112) from 5% to 7.5% and on Zinc Oxide (HS 281700) from 7.5% to 10%

Indian primary zinc industry is going through a tough time with input costs increasing year on year due to higher exploration costs, mining expenses, lower concentrate treatment charges, coupled with the increased royalty charges and falling concentrate charges and falling concentrate grades. Thus smelting of Zinc metal is becoming a costly affair with revenue generation capability being limited as pricing is based on an index (LME). Zinc producers are 'price takers' and do not have control on fixing of prices.

For some applications like die casting and Zinc Oxide, Zinc scrap is being imported which leads to an inferior quality of die casting at a cheaper cost. This poses serious threat to organized die cast alloy producers. Import of Zinc scrap has significantly increased by more than 100% since Financial year 2010-11, and rendered the high quality manufacturers of Zinc downstream products uncompetitive. It is therefore recommended that the Government may increase the basic customs duty on Zinc Ingots (HS 790111/12) from 5% to 7.5% and on zinc oxide (HS 281700) from 7.5% to 10%.

3.17.16. Increase the duty drawback rate on Zinc Ingots (HS code 790111, 790112) to 3% from existing 1.5%

Nearly one lac tonne of production capacity in primary Zinc Ingots is lying idle in India for want of adequate demand. However, the international Zinc market is extremely competitive and high ocean freights for major Zinc markets from India make the competition scenario further prominent. An important support mechanism in boosting the export volume from India is the duty drawback rate. The All Industry Rate (AIR) of duty drawback on Zinc ingots (HS Code 79011100, 79011200) is currently 1.5%. Zinc industry is incurring higher duty incidence (non-cenvatable) on the raw materials consumed in the manufacturing of finished export goods and the recovery of duty in the form of currently available duty drawback rate of 1.5% is insufficient. This increase would just be sufficient to offset the duties on the input materials being consumed for the manufacture of finished Zinc ingots. It is accordingly

recommended that duty drawback on zinc ingots (HS 790111/12) be increased from 1.5% to 3%.

POWER

GST

3.18.1. Electrical Energy should be considered under taxable goods category with tax rate of 5% or below

Under GST, Electrical Energy is NIL rated goods covered under Chapter Heading 2716 00 00 under Schedule I. As per section 17 of the CGST Act, amount of GST paid on inputs shall not be allowed as credit wherein such inputs are used for effecting exempt supplies. Due to this, entire GST suffered on inputs by the power companies is not eligible for credit and results in to cost of generation of electricity. It is recommended that electrical energy should be considered as taxable goods with tax rate of 5% or below under the GST regime. This would entitle power generation companies to avail input tax credit on all the inputs/input services used for power generation. This shall make the cost of power generation lower, ultimately resulting into cheaper power for the consumers.

3.18.2. Custom duty on coal for consumption in Thermal Power Plants

At present, coal imports are subject to BCD of 2.5% and IGST of 5%. Since there is shortage of domestic coal in India, power plants are compelled to meet the requirement through imports. Since there is no duty on electricity on the output side, any duty imposed on procurement of coal would be a cost for power companies. The present duty structure is unintentionally increasing the cost of power generation and thereby increasing the cost of power, which is directly impacting the common man. It is recommended that BCD and IGST on coal imported for the usage in thermal power plants should be NIL. Without prejudice to the above, IGST @5% on coal shall be reduced to 2% to bring it in line with levy of CVD being levied on the same goods under erstwhile indirect tax regime.

DIRECT TAX

3.18.3. Extension of Tax Holiday to Power Companies

Issue

Power is the critical infrastructure on which the socio-economic development of any country depends. So a clear and stable tax regime is bare minimum requirement of the investors/developers engaged in development of power plants. The companies engaged in development of power plants were eligible for deduction under section 80-IA of the Act. However, the same is set to expire on 31st March 2017. The Finance Act 2016 has allowed investment linked deduction for the capital expenditure incurred on “infrastructure facility” by inserting provision in section 35AD of the Act. However, the definition of ‘infrastructure facility’ as per section 35AD of the Act does not include power sector and hence companies in the power sector will be deprived of any such benefit under section 35AD of the Act. The definition of ‘infrastructure facility’ specifically includes road, railways, housing, water supply project, port, airport, inland waterway etc. hitherto being eligible for deduction under section section 80-IA of the Act. Considering the thrust of the government on “power

for all" this is certainly not intention for the sector which is already reeling under cost escalation due to GST, resulting in higher price to the consumer.

Section 80-IA of the Act provides deduction in relation to profits of certain undertakings. It was well settled that in the case of restructuring of any entity owning such undertaking, the benefits of deduction will be available to entity owning the undertaking post restructuring. Sub-Section (12) of section 80-IA provided that in the year of restructuring deduction will not be allowable to the transferor entity but same will be allowed to the transferee entity as it would have been allowed, had the restructuring not taken place. However, sub-section (12A) was inserted in Section 80-IA of the Act with effect from 1st April, 2008 to provide that nothing contained in sub-Section (12) shall apply to reorganization post 1st April, 2007. A view is expressed that post insertion of sub Section (12A), benefit of deduction under Section 80-IA of the Act will not be available to the amalgamated/resulting entity.

Recommendation

To keep parity and growth of infrastructure which is one of the priority areas of the Government, it is suggested that generation or generation and distribution of power covered by provisions of section 80IA of the Act should also be covered by section 35AD of the Act. Alternatively, it is suggested that the benefit of deduction under section 80IA of the Act be continued for power sector undertakings and appropriate amendments be made in section 80-IA of the Act. It is further suggested that section 80-IA(12A) of the Act be deleted to enable restructuring of eligible entities or Section 80-IA(12) of the Act should be amended to provide for allowing deduction to the amalgamating/demerged entity for the period till transfer date and to the amalgamated/ resulting entity post transfer.

PUBLISHING

3.19.1. The applicability of GST on reverse charge basis on royalties payable to authors is creating numerous challenges for the publishers. While there is no output tax on the print books/journals supplied by the publisher, the publisher ends up incurring additional cost by way of reverse charge on royalties paid to the authors. Under the erstwhile service tax regime, royalties on original literary work was exempt. However, under GST regime, GST is an additional cost to the publisher as the output is tax-free and the input tax credit cannot be availed on the print books/ journals. The principle of taxing royalties under GST does not seem to be in alignment with international practices. The new additional tax element increases costs in the hands of the publisher, who, in turn, has to modify the product pricing to absorb the tax cost. Price increase, and that too, for commodities like academic books is against the intent of the Government. It is accordingly recommended that the requirement of applicability of GST on reverse charge basis on royalties be removed particularly when it was not applicable under the service charge regime also.

PULP, PAPER AND PAPER BOARD

3.20.1. Re-impose Customs Duty on Paper and Paperboard

The domestic paper and paperboard industry has already made significant capital investments to ramp-up capacities, the gestation period is long and the economic viability of

the investments are impacted significantly by availability and cost of raw materials and other inputs. Even as the industry is grappling with the issue of producing paper and paperboards at competitive costs, the problem has been exacerbated by the Government's policy of extending preferential tariff treatment to paper and paperboards under the FTAs and other bilateral and multi-lateral trade agreements and pacts. Further, the economic slowdown in developed economies and export dependent economies like ASEAN countries has led to severe excess capacity of paper and paperboard in these countries. Taking advantage of the low import duty rates, these countries find India as an attractive outlet for diverting their excess inventory. The scenario has become grimmer with the basic customs duties on most of the paper and paperboard coming down to nil rate from 01.01.2014 under the India-ASEAN FTA. As a result imports into India will further accelerate in view of higher capacity creation in China and ASEAN countries. It has to be ensured that the capital already invested and proposed to be invested in further capacity creation by Paper and Paperboards industry in India is safeguarded, incentivized and grown further. It is suggested that customs duty on import of paper and paperboard from ASEAN countries should be re-imposed at rates similar to those applicable on imports from non-ASEAN countries. Further, in order to provide a level playing field to the domestic industry, Paper and Paperboard products should be kept in the Negative List (i.e., no preferential treatment) while reviewing the existing FTAs and formulating new FTAs.

3.20.2. Customs Duty on Import of Pulp

In May 2012 the Government reduced the import duty on pulp from 5% to "Nil". It is estimated that more than 1.25 million MT of pulp, valued at approximately USD 710 million (about Rs. 4,600 crore) is imported in to the country every year. The customs duty foregone on account of these imports is estimated to be about Rs. 245 crore p.a. The break-up of the pulp imports is as under:-

Type of Pulp	Quantity ('000 MT)	Value (Rs. Crore)
Hard Wood Chemical Pulp	900	3,420
Soft Wood Chemical Pulp	200	900
Bleached Chemi Thermo Mechanical Pulp (BCTM Pulp)	160	580
Total	**1,260**	**4,580**

It is submitted that if domestic production of pulp is encouraged through measures including imposition of Customs Duties on pulp imports, not only will it provide a fillip to creation of jobs, it will also have a salutary effect of overall economic development of the vast rural hinterland that houses the pulpwood plantations.

In view of the fact that Soft Wood cannot be grown in the country, requirement of Soft Wood Pulp will have to be met through the import route only, justifying the exemption from Customs Duty. However, in so far as Hard Wood Pulp is concerned, it would be pertinent to

note that the domestic industry is working closely with the farming community for creating sustainable supply of wood – a key raw material for hard wood pulp – through re-development of waste-lands.

In so far as Bleached Chemi Thermo Mechanical Pulp (BCTMP) is concerned, the technology for manufacturing BCTMP has not been available in India. In line with the vision "Make in India" of Hon'ble Prime Minister, the paperboards industry has, for the first time in the country set up a state of art BCTMP manufacturing facility which is operational since March 2017**.** This project will save in perpetuity substantial quantum of forex outflows that would otherwise be spent for import of BCTM pulp.

In an era of increasing global competition it is necessary for governments and industry to work in partnership to ensure creation of economic wealth for the nation. Accordingly, to energise creation of sustainable sources of fibre required by the pulp and paper industry it is recommended that**:**

a) policy measures be put in place to facilitate private sector participation in plantation development programmes and

b) 10% customs duty on pulp be imposed only for Hard Wood Chemical Pulp and Hardwood Bleached Chemi Thermo Mechanical Pulp (BCTMP) by sub-classification of the existing Tariff classification 47050000 (Bleached Chemi Thermo Mechanical Pulp, (BCTM Pulp)} in to Hardwood BCTMP and Softwood BCTMP.

3.20.3. Reduction of GST on Poly-Coated Paper and Paperboards

Raw material for paper cups is paperboards primarily manufactured from wood species such as eucalyptus, subabul and casurina. Environmentally responsible Paper Mills in India source these species of wood from sustainably managed social and farm plantations. Environmentally responsible Paper Mills in India source these species of wood from sustainably managed social and farm plantations. From the perspective of eco-friendliness and reduction of carbon footprint the usage of paper cups is a preferred option.

Paper and paperboard that is coated / impregnated / covered with poly coating are classified under Tariffs 4811 51 90 *(Bleached, weighing more than 150 g/m2* - Other*)* and 4811 59 90 (*Other* - Other) with GST of 18% ad valorem – even as a large number of paper/paperboard items covered by Tariff 4802, 4804, 4805, 4807, 4808 and 4810 are taxable to GST only at 12% ad valorem. In India major consumers of coated/ poly-coated paper/paperboards are small units, who are increasingly supplying to institutional customers like the Railways, the FMCG sector and the Household sector. Paper cups are used for mass consumption items such as tea, coffee, fruit juices, soft drinks, ice cream etc.

The Poly coating is necessary for manufacturing of paper cups /glasses as the coating acts a sealing /binding medium and makes cup/glasses moisture proof against hot/cold beverages. Typically, poly-coated paper contains paper and poly at a ratio of 92:8 and thus, poly-coated paper merits levy of GST at a lower rate.

It is, thus, recommended that GST on poly coated paper / paperboards, classifiable under Tariffs 4811 51 90 (Bleached, weighing more than 150 g/m2 - Other) and 4811 59 90 (Other

- Other) is reduced to 12% from 18% - in line with most other paper/paperboards classifiable under Chapter 48. Such a move will also be a "green" initiative in line with global trends**.**

3.20.4. Incentives for Investments in Environment Friendly "Clean" Technologies by Paper Industry

Indian Pulp, paper and paperboard Industry is a signatory to the Government of India's Charter on Corporate Responsibility for Environmental Protection (CREP). This calls for substantial investments in green technologies such as introduction of ECF (Elemental Chlorine Free) pulp manufacture, Ozone bleaching etc. to ensure a positive environmental footprint. The domestic manufacturers are consciously focusing on clean technologies which involves significant capital investment, to ensure compliance & improve performance in the area of environment, without much return from such investments. Hence such investments affect the profitability/viability of the business.

Hence, in order to encourage manufacturers within the industry to adopt environment friendly "clean" technologies that ensure, inter-alia, reduced carbon footprints, better emission norms, better effluent treatment norms, usage of renewable sources of raw material and energy, improved waste recycling, etc., appropriate fiscal benefits should be provided.

It is recommended that:-

a) Import of capital goods required by the Paper & Paperboard industry for technological up-gradation - specially aimed at environmental protection (e.g. Elemental Chlorine Free Technologies) and for compliance with CREP - be permitted at 'Nil' rate of Customs Duty.

b) Exports by manufactures who have adopted environmentally friendly technology are granted additional incentives in the form of cash incentive of 5% of FOB.

c) Following additional benefits are provided for paper board industry for investing in clean technology:-

   i. Entitlement for import of all raw materials at a 50% concessional rate of duty;

   ii. Full exemption from GST for paper and paperboard produced using clean technology;

   iii. Accelerated tax depreciation under the income tax law for investments in environment friendly technology.

These measures will not only promote preservation of ecology, it will also incentivise all players in the Indian Paper Industry to adopt 'green' technologies, thus aligning domestic industry to international eco-friendly norms**.**

3.20.5. Provide clarity on HSN code for pulpwood used for making Pulp

Wooden chips used for manufacture of pulp is sourced from pulpwood trees of different species like Eucalyptus, Casuarina and Subabul. The wood from these trees are sourced

from agro and farm forestry plantations. For ease of transportation the pulpwood is transported from the plantations in log form and thereafter chipped and 'cooked' at the paper-mills for the purpose of pulp-making.

In the pre-GST regime, the pulpwood was exempt from Central Excise duty by virtue of being a farm produce. VAT was levied @ 5% by certain State Governments on the Eucalyptus pulpwood under the VAT Schedule Heading – "Bamboos, Casuarina poles, Eucalyptus logs and cut sizes thereof."

Under GST regime, there is no specific heading that covers pulpwood like Eucalyptus, Casuarina and Subabul. The consequent lack of clarity in this regard has given rise to confusion regarding applicable tax on supply of the said pulpwood. In the absence of a specific clarification in the matter pulpwood may be treated as a "residuary item not specified elsewhere" and charged to tax at the highest rate.

Under Schedule I of GST (tax @ 5%) HSN 4401 covers "Wood in chips or particles, saw dust and wood waste and scrap, whether or not agglomerated in logs, briquettes, pellets or similar forms."

Considering the fact that pulpwood is essentially waste/scrap wood that is used for pulp making, classification of the same under Schedule I (HSN 4401) bearing GST @ 5% appears to be the correct classification. This would also be in alignment with the pre-GST tax rate applicable on Eucalyptus logs and cut sizes. Moreover, the pulpwood chips are used as inputs for making wood pulp which is classified under Schedule II (HSN 4705) - "Wood pulp obtained by a combination of mechanical and chemical pulping processes" attracting GST @ 12%. In case pulpwood is charged to tax at the highest rate of GST it would lead to an avoidable situation of an inverted duty structure.

It is recommended that appropriate clarification be issued to the effect that pulpwood (hitherto charged to VAT only @ 5%) is classifiable under HSN 4401, chargeable to GST @ 5%.

RENEWABLE ENERGY

3.21.1. Provide Exemptions to Renewable Energy Sector under GST regime

The current tax exemptions provided to the renewable energy sector should be continued under the GST regime as well. In addition even the services rendered to a project owner for setting up and operation of renewable energy plant/project should be exempt from levy of GST. This would ensure that there is no adverse impact on the procurements made for generation of renewable energy due to increase in tax costs. The project developer should be eligible to claim refund of GST paid (both at Central and State level) on goods and services used for setting up and operating renewable energy project. Alternatively, sale of goods and services to renewable energy projects should be zero rated, i.e. the vendors providing such goods and services at nil GST rate should be eligible to avail credit of the GST paid on inputs, capital goods and services used.

3.21.2. Applicability of GST on Renewable Energy Certificates

Renewable Energy Certificate (REC) is a market based instrument to promote renewable energy generation. The Electricity Act, 2003, the policies framed under the Act, as also the National Action Plan on Climate Change (NAPCC) provide for a roadmap for increasing the share of renewable in the total generation capacity in the country. It is aimed at addressing the mismatch between availability of RE resources in state and the requirement of the obligated entities to meet the renewable purchase obligation (RPO). Central Electricity Regulatory Commission (CERC) has notified Regulation on Renewable Energy Certificate (REC) to promote renewable sources of energy and development of market in electricity.

The framework of REC is expected to give push to RE capacity addition in the country. The REC framework seeks to create a national level market for renewable entities generating RE to recover their cost. The REC incentives can be exchanged only in the Power Exchanges approved by CERC within the band of a floor price and a ceiling price to be determined by CERC from time to time.

However, unlike exemption from GST provided to incentives like MEIS and SEIS Scrips under the Foreign Trade Policy for promotion of exports, no such exemption has been provided to RECs which are meant for promotion of generation of renewable energy in the country.

It is recommended that in order to encourage increase in the renewable energy generation capacity in the country full exemption from GST be provided to Renewable Energy Certificates.

3.21.3. Supply and installation of solar roof top under EPC contract to be considered as supply of power generating system @ 5%

The supply and installation of solar roof top, supply of solar power project and installation of the same is considered as works contract service (in relation to immovable property) attracting 18% GST. However, renewable energy devices and parts for their manufacture are subject to GST @ 5% classified under Chapter 84 and 85. The composite supply of works contract is also subject to tax at the rate of 18% under the GST regime. Tax at the rate of 18% under the GST regime on the supply and installation of solar roof-top and solar power project would lead to additional burden of tax. It is suggested that appropriate clarity be provided that supply and installation of solar roof-top shall be construed as supply of solar power generating system liable to tax @ 5% under the GST regime. Appropriate clarity be also provided on whether solar power generating system mentioned under chapters 84 & 85 are for all projects irrespective of the capacity size.

3.21.4. Prescribe concessional rate of GST of 5% on solar based agricultural and drinking water pumps

Solar based agricultural pumps and solar based drinking water pumps (off-grid systems) are essentially solar based devices. It is requested that appropriate clarity be provided with regard to applicability of 5% rate of GST on solar based agricultural pumps and drinking water pumps (being solar based devices) and on the applicable HSN Code.

DIRECT TAX

3.21.5. Prescribe higher rate of depreciation to renewal energy devices

Currently the rate of depreciation on the specified renewable energy devices under New Appendix I read with Rule 5 of the Rules was brought down to 40% by the Income-tax (Twenty Ninth Amendment) Rules, 2016, w.e.f. 1-4-2017. It is suggested that the rate of depreciation on renewable energy devices be reinstated to 80%-100%.

STEEL AND OTHER FERROUS PRODUCTS

3.22.1. Increase in Import Duty on Stainless Steel Products to 15%

The current import duty on Stainless Steel Products in India is at 7.5%, which is much lower in comparison to duty prevailing in other stainless steel producing countries. This has led to increased imports from 324,460 MT in 2013-14 to 532,033 MT in 2015-16. Imports from China have more than doubled from 111,765 MT in 2013-14 to 276,456 MT in 2015-16. China now accounts for more than 50% of the import basket. This is the single largest threat for the stainless steel industry today.

Also, in view of the comparative advantage enjoyed by China in various cost components, it is imperative to create a level playing field between domestic stainless steel manufacturers and the Chinese manufacturers.

Therefore the Basic Customs Duty on stainless steel flat products need to be increased from the existing 7.5% to 15%. Also, in order to safeguard the huge investment made towards the development of the Indian stainless steel industry, the peak duty rates for stainless steel may be raised to 25% from the existing 15%.

3.22.2. Increasing Basic Custom Duty on Steel Products

In the Union Budget for 2015-16, the government had increased the tariff rate on steel products (long and flat products) to 15%, however, the duties are still only 10% on Long Products and 12.5% on Flat Products. But, with imports still high at 7.4 MT for 2016-17, we recommend for increasing the import duty on steel products to 15% for both long as well as flat.

3.22.3. Exemption of Import duty on Ferrous and Stainless Steel Scrap

Ferrous and Stainless Steel Scrap is not available indigenously in sufficient quantities. So, the domestic steel companies have to rely on imports of this key raw material. Imposition of import duty on the scrap, increases the raw material cost adversely affecting the steel manufacturers' competitiveness.

Therefore, we recommend that Import duty on Ferrous and Stainless Steel Scrap (HS Code: 7204 49 & 7204 21) should be reduced from the existing rate of 2.5% to 'NIL'

3.22.4. Reduction of Basic Customs Duty on Metallurgical Coke to NIL

Basic Customs Duty on metallurgical coke has been placed at 5%. Coking Coal, Steam Coal and Met Coke are key inputs in steel making, accounting for substantial portion of cost of production for steel. Historically, coal used for metallurgical purposes have enjoyed

exemption as steel is critical in fuelling India's growth. The coke prices have surged sharply in recent months. If the duty is reduced, it will help the domestic steel industry to be cost competitive. Therefore, we suggest a reduction of Basic Customs Duty on metallurgical coke to NIL.

3.22.5. Exemption from Import duty on Pet Coke

Pet coke (2% Sulphur) is gaining importance as one of the important carbon bearing inserts used by Steel Industry, part replacing costly and scarce coking coal and adding carbon value to the end product i.e., metallurgical coke by increasing the carbon content and yield of coke in turn reducing imports of costly metallurgical coke. Pet coke (2% Sulphur grade) is a relatively cheaper substitute of Met Coke and should therefore be encouraged in domestic industry to help save precious foreign exchange and make domestic steel mills more competitive by lowering their cost of production.

It is therefore recommended that Customs Duty on Pet coke (CTH 2713) be reduced from 2.5% to NIL.

3.22.6. Reduction in Customs Duty on Coking Coal to NIL

Coking coal is used largely by the steel industry. Negligible quantity of coking coal is available domestically, and thus the need is met mainly from imports. The zero duty on coking coal was in place since 1978. However, its increase to 2.5% in the Union Budget 2014-15 has increased the cost of steel making substantially and has rendered the domestic steel being uncompetitive vis-à-vis imports. It is therefore recommended that the customs duty on coking coal (HS Code: 2701 19 10) be reduced to Nil from 2.5%, as was the case earlier.

3.22.7. Exemption from Import Duty on Anthracite Coal

Anthracite Coal, Coking coal, Coke, Pet Coke, Limestone, Dolomite are vital Inputs for the steel Industry. The availability of these items in good quality is declining in the country and the Industry has to depend on their imports on regular basis. The basic Customs Import Duty on Anthracite Coal is 2.5%. Since Ferro Alloy Industry plays a vital role in the manufacturing of steel, it is necessary to make available these reductants at international competitive price to make Indian steel mills more competitive.

It is therefore recommended that Customs duty on Anthracite Coal (CTH 27011100) be reduced from 2.5% to NIL.

3.22.8. Reduction of Import Duty on Steel Grade Limestone and Dolomite to NIL

For Indian steel industry, the cement grade limestone reserves are adequate but the reserves of SMS, BF and Chemical grade limestone are not adequate and are also available in selective areas. Increase in steel production in the country, has led to rising demand for SMS and BF grade limestone. Therefore the limestone imports have been increasing consistently. It is imperative that Customs Duty on steel grade limestone (sub heading 2521 00 10) and dolomite (sub heading 2518 10 00) be reduced from 2.5% to NIL.

3.22.9. Imposing 30% Export Duty on exports of Graphite Electrodes

The rising demand and reduction in capacities in the global market has created acute shortage of graphite electrodes domestically. Non-availability of this may result into shutdown of Electric Arc Furnace steel units as it is inevitable consumable for melting scrap.

It is recommended that 30% export duty on Graphite Electrodes be imposed to increase its domestic availability vis-à-vis export.

3.22.10. Reduction of Customs Duty on Natural Gas to NIL

India has a gas based steel manufacturing capacity of 10-12 MTPA accounting for almost 8-9% of the total steel manufacturing capacity in the country. The gas based units in western coast of the country were the earliest gas users and have contributed in a big way in nurturing the gas and steel industries during their nascent years. These plants were set-up pursuant to 5.46 MMSCMD of domestic gas allocation by Gas Linkage Committee (GLC), Government of India between 1991 & 2002 and 4.20 MMSCMD by EGOM in 2009 on priority to compensate for APM gas supply curtailed. However, the units today are facing unprecedented challenges for their sustainability due to non-availability of affordable natural gas.

Due to the non-operations of these units, it has to face adverse effects such as stranded investment and unemployment. It is essential that customs duty on LNG is made NIL without “Any User Condition” so that user industries including Gas Based Steel Plants are able to import LNG for usage in making of steel.

3.22.11. Customs Duty on Seconds and Defective Goods falling under Chapter 72

Prime quality of major finished steel products are liable to customs duty at 12.5% on flat and 10% on long products. However, seconds and defective goods falling under Chapter 72 of the Customs Tariff are liable to customs duty @ 15%. In view of the narrow margin of difference between the rates of import duties of prime quality and seconds / defective goods, there has been a surge of imports of ‘seconds’ and ‘defective’ steel products in the country. This is putting pressure on the industry already grappling with the challenge of subdued demand and rising cost of production; alongside raising the quality concerns for long-term infrastructure and construction projects using steel. In order to suppress the imports of defective steel into the country, the rate of seconds / defective goods needs to be increased. It is suggested that customs duty on seconds and defective goods falling under Chapter 72 be raised to 40%.

3.22.12. Reduction in Customs Duty on Ferro Nickel, Pure Nickel and Ferro Moly to NIL

Stainless steel is made of combination of iron, chromium, silicon, nickel, carbon, nitrogen, and manganese. Properties of the final alloy are tailored by varying the amounts of these elements. It is a highly raw material intensive industry with over 70% of the cost being accounted for by raw material and therefore adequate raw materials availability is critical for this industry. The key ingredients for production of stainless steel include Ferro Nickel, Pure Nickel, Ferro Moly etc. These are not available in India and need to be necessarily imported for production of stainless steel.

Therefore, the Basic Customs Duty on all key raw materials like Ferro Nickel, Pure Nickel, Ferro Niobium, Ferro Vanadium, Ferro Titanium and Ferro Moly be reduced to zero to ensure that domestic industry remains competitive globally. It would also help the Indian stainless steel manufacturers to pursue a more aggressive export strategy since they would be cost competitive in the international markets.

3.22.13. Royalty and all other taxes to be subsumed in GST

The prices of iron ore, a key raw material for the steel industry, are already moving upwards. On and above these high ore prices, domestic steel producers need to pay for high royalty and other taxes and cess like District Mineral Fund etc. adversely impacting comparative cost competitiveness of Indian steel manufacturers. Therefore, royalty and all other taxes, cesses, etc. should be subsumed in GST.

TEXTILES

3.23.1. Custom duty Structure for Polyester and Nylon value chain

Polyester is the key pillar of India's robust synthetic fibre industry. Indian manufacturers have made substantial investments in creating domestic capacities of fibre intermediates like PTA and MEG. However, massive surplus capacity of PTA and MEG in other countries pose a serious threat to these investments today. The recommendations relating to the proposed custom duty in the polyester value chain is given below for consideration of the Government:

Item	Customs duty (%)		
	Tariff No.	Present	Proposal
PTA	291736	5	5
MEG	290531	5	5
Polyester chips	39076010 and 39076020	5	7.5
Polyester staple fiber	5503 20	5	10
Polyester filament yarn	5402 33	5	10
Polyester high tenacity yarn	5402 20	5	10
Polyester tyrecord fabric	5902 20	5	10

The recommendations relating to the proposed custom duty in the nylon value chain is given below for consideration of the Government:-

Item	Customs duty (%)		
	Tariff No.	Present	Proposal
Caprolactam	2933 71	7.5	5

Nylon Chips	3908 10	7.5	7.5
Nylon Filament Yarn	5402 45	7.5	10
Nylon High Tenacity Yarn	5402 10	7.5	10
Nylon Tyrecord Fabric	5902 10	10	10

3.23.2. Rationalize Customs Duty on Knitted Fabric

Chapters 54 and 55 of the Customs Tariff specify Customs Duty of 10% + Specific duty depending on the items. However, Chapter 60 (knitted fabric) does not provide for specific duty. Consequently a large quantity of fabric is being imported as Knitted fabric. To prevent the misuse it is recommended that Chapter 60 of the Customs Tariff should also have the same provisions as that of Chapters 54 & 55 - Custom Duty of 10% + Specific Duty.

3.23.3. Revise Basic Custom Duty on import of Flax/Linen Yarn

The BCD on Flax/Linen Yarn stands at 10%. Before the implementation of GST, the protection to domestic flax / linen yarn industry was to the extent of 29.44% which has reduced to 10.3% as given below:-

Computation of CVD+SAD impact on Flax/Linen Yarns (HS 5306)

(a) Taxation Impact on Imports under Pre-GST Regime

Particular	**Duty rate %**	**INR**
Assessable Import Value		**100.00**
Add: Basic Custom Duty @ 10% (BCD)	10.0%	10.00
Add: CVD @ 12.5% *(On Import Price + BCD amount)	12.5%	13.75
ADD: Education Cess @ 3% * (On BCD + CVD amount)	3.0%	0.71
Add: AED/SAD @ 4% *(On Import Price + BCD + CVD + Education cess amount)	4.0%	4.98
Total		**129.44**

Total incidence of protection to domestic industry against import - 29.44%

*No credit for CVD+SAD/AED was availed by the spinners and weavers since they were exempted from payment of excise duty on yarn and fabric in pre-GST regime.

(b) Reduced Protection under Post-GST Regime

Particular	**Duty rate %**	**INR**
Assessable Import Value		**100.00**
Add: Basic Custom Duty @ 10% *(BCD)	**10.0%**	**10.00**
Add: Education cess @3% *(BCD amount)	**3.0%**	**0.30**

Total		**110.30**

Total incidence of protection to domestic industry against import - 10.30%

(5% IGST not factored as input credit for the same is available)

Difference on account of abolition of CVD + SAD	19.14% (a-b)
Add Impact of price drop by China	20.00% (Since August '16)
Total adverse impact	39.14% or Rs. 250/-per kg (based on commonly consumed yarn count i.e. 36 Nm and Above)

Accordingly, there is a need for revision of BCD on Flax/Linen Yarn (HS-5306) to neutralise the negative impact caused by abolition of protective CVD and SAD levy on imports under GST regime.

3.23.4. Basic Custom Duty on Viscose Based Products

India is facing stiff competition from lower cost textile producing countries. There has been an increase of viscose spun yarn import from China & Indonesia to India in the recent years because of overcapacity & lower cost of production, thus affecting domestic spinners in India. Both at yarn and fabric stage, import price is cheaper as compared to domestic prices. Following are the key suggestions:

- Increase BCD from nil to 5% in case of Indonesia, as there is no import duty on VSF import from Indonesia under India–ASEAN FTA. This needs to be revisited and renegotiated. Increase import duty from 5% to 10% for imports from other countries.
- Increasing BCD from 5% to 10% on viscose spun yarn in the interest of domestic spinners.

DIRECT TAX

4.1. Tax Rates – Companies/Firms/Limited Liability Partnership

Issues

- Businesses today are faced with high tax cost leading to increased cost of production and resultant lower surplus for reinvestment and expansion. The basic corporate tax rate of 30 percent coupled with dividend distribution tax rate of 20% makes the effective tax cost for an Indian company too high. In addition to this, lowered depreciation rates, lead to increased pay-out of taxes thus leaving inadequate funds for generation of internal resources for ploughing back for expansion, modernization, technology up-gradation, etc. The Finance Minister while presenting Budget 2015-16 promised that the rate of corporate tax will be reduced from 30 per cent to 25 per cent over the next four years with corresponding phasing out of exemptions and deductions. The Finance Act, 2016 phased out many exemptions and deductions however, the rate of tax was reduced to 29% only for domestic companies having total turnover or gross receipts in the previous year 2014-2015 upto Rs. 5 crore. Further, the Government through the Finance Act, 2017 choose to restrict the reduction in tax rate to smaller companies only. The rate of tax for a domestic company was reduced to 25% if the total turnover or gross receipts in the previous year 2015-2016 does not exceed Rs. 50 crores. Thus, there is a huge strain on companies not falling within the turnover criterion of Rs. 50 crores.
- In respect of corporate tax rate of 25% for domestic companies having total turnover/gross receipts not exceeding Rs. 50 crores in the previous year 2015-16, it is not clear as to whether the companies who have started business during the financial year 2016-17 or financial year 2017-18, would be eligible for the lower tax rate of 25%, in case the total turnover/gross receipts in the year of operation do not exceed Rs. 50 crores. It would be unfair if the benefit of reduced tax rate is not allowed to these smaller companies merely because they started operations in the aforesaid financial years.
- It is also observed that most of the deductions and exemptions phased out by the Finance Act, 2016 are applicable to both companies as well as firms/Limited Liability Partnerships ('LLPs'). However, the benefit of reduction of tax rate is not passed on or being considered to be passed on to such other assessees. The rate of tax for firms and limited liability partnership is considerably high and needs to be reduced to 25% in sync with the reduction in corporate tax rate and phasing out of deductions and exemptions. This would facilitate ease of doing business in any form and not particularly restrict the benefit to corporates.
- The Finance Act, 2015 increased the rate of surcharge by 2 per cent if the income exceeds a specified threshold (10 crores in case of a domestic company and 1 crore in case of a Firm). The increased rate of surcharge on tax makes cost of doing business in India significantly high. The increased tax cost adversely impacts the investors' sentiments and economic growth.

Recommendations

- It is requested that the Government should reduce the corporate tax rate across the board to 25% and announce a road map for its reduction especially after phase-out of deductions and incentives.
- It is suggested that the reduced tax rate of 25% should be extended to companies who have started business either during the financial year 2016-17 or 2017-18 and if their total turnover/gross receipts in the first year of operation do not exceed Rs. 50 crores.
- It is suggested that the Government should clarify and extend the benefit of reduced tax rate of 25% to those entities that existed as firms during the financial year 2015-16 and subsequently converted into companies.
- It is further suggested that the MAT on such companies should also be reviewed/reduced to make the relief truly meaningful.
- The income tax rates for unincorporated bodies i.e. Firm, Limited Liability Partnership (LLPs), etc., should also be reduced to 25% from the current 30%.
- It is recommended that the Corporate Tax rate of 25% should be after inclusion of surcharge and education cess.
- The rate of Dividend Distribution Tax may also be reduced suitably so as to be competitive in terms of the comprehensive tax burden.
- It would be appropriate to remove the levy of surcharge and education cess on corporate and non-corporate taxpayers.

4.2. Tax Rates - Individual Taxpayers

Currently, the peak tax rate of 30% is made applicable over an income of Rs. 10 lakhs for individual taxpayers. However, the income level on which peak rate is applied in other countries is significantly higher. Hence, there is a need for further raising the income level on which the peak tax rate would trigger, to make the same compatible with the international standards.

FICCI recommends the following revised tax slabs for individual taxpayers. FICCI would, therefore, like to urge that the aforesaid recommendation be implemented during FY 2018-2019.

Slab (Rs. lakhs)	Tax rate
0-3	Nil
3-10	10%
10-20	20%
Beyond 20	30%

The Finance Act, 2016 has levied surcharge @ 15% on individuals having total income exceeding Rs. 1 crore. Further, the Finance Act, 2017 has levied surcharge @ 10% on individuals having total income exceeding Rs. 50 lakhs but not exceeding Rs. 1 crore.

Individuals with income above Rs. 1 crore would be subject to surcharge @ 15% on tax. The surcharge @ 10% on individuals having taxable income above Rs. 1 crore was introduced in the Budget 2013-2014 though only for a year. The surcharge on individuals has been increased over the years from 10% to 15%. It is observed that the increased surcharge on certain category of individuals distorts equity and tends to discourage entrepreneurship and incentivizes people to relocate to other locations. It is suggested that the Union Budget 2018-2019 should completely withdraw the levy of surcharge on individuals.

4.3. Minimum Alternate Tax and Alternate Minimum Tax - Section 115JB/115JC

Issues

- The purpose behind introduction of Minimum Alternate Tax ('MAT') was to bring all zero tax companies and to neutralize the impact of certain benefits/incentives. With phasing out of exemptions and incentives under the Act, the current rate of MAT of 18.5% is quite high and has impacted significantly cash flow of companies who otherwise have low taxable income or have incurred tax losses. MAT has also diluted significantly the tax incentives offered under Chapter VI-A of the Income-tax Act,1961 (the Act) to eligible businesses and Industrial Undertakings as the difference between the effective tax rate based corporate tax rate at 30% and MAT at 18.5% is not very large.
- Any exercise for revival of stressed assets typically involve restructuring of the debt as a plan of resolution process which may give rise to 'notional' gain/benefit on account of write-back of liability in the books of accounts. It has historically been recognised that any gain/ benefit which is derived by an assessee from an approved scheme of insolvency is kept outside the purview of MAT. However, currently, there is a widespread concern that any write back of liability (on account of compromise or other arrangement) in books of accounts by a distressed corporate debtor pursuant to an approved repayment plan under Insolvency and Bankruptcy Code (IBC) could result in an artificial increase in book profit. This in turn may lead to a levy of MAT on such fictional income. Such tax costs in turn, could undermine the very purpose of IBC by making schemes costly and financially unviable. It may be noted that similar schemes dealing with sick companies in the past [for instance, a scheme under Sick Industrial Companies (Special Provisions) Act, 1985 ('SICA')] enjoyed exemption from levy of MAT. SICA has been repealed, and consequently Board for Industrial and Financial Reconstruction (BIFR) stands abated with effect from December 1, 2016. All references made or pending with BIFR at any stage therefore also stand abated. In view of this, the relief available against MAT to Sick Industrial Companies under section 115JB of the Income Tax Act,1961 ('the Act') shall no more be available. This is an unintended consequence of repealing of Sick Industrial Companies (Special Provisions) Act, 1985.
- 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. Even the provisions of the Companies Act, 2013 allows entire brought forward loss including unabsorbed depreciation for set-off from current year profit for the purpose of computing allocable surplus for dividend. A company

having huge book losses and meagre unabsorbed depreciation or vice versa would be adversely affected and would end up paying MAT despite having huge accumulated losses. This causes undue hardship to revive companies and hampers the revival process substantially.

- Further, the Act does not provide the methodology to compute the amount of loss brought forward or unabsorbed depreciation as per books of accounts for the purpose of claiming deduction while computing book profit under section 115JB of the Act. The issue has created unwarranted litigation and needs to be resolved.
- An Alternate Minimum Tax (AMT) was also introduced on LLPs, individuals, HUF, AOP etc. which is to be computed on adjusted total income. Adjusted total income is total income as increased by deduction claimed under Chapter VI-A and Section 10AA of the Act and under section 35AD of the Act (net of depreciation).

  Pursuant to above, LLP's who have invested large sums in eligible businesses/industrial units in the backward areas are also getting penalized as the benefit of such incentive gets reduced.
- The MAT/AMT credit is allowed to be carried forward for 15 years for set-off but this period is generally not always sufficient. Many companies are not able to utilize MAT credit efficiently and within due time-limits provided.
- Income arising from the transfer of a long-term capital asset, being an equity share in a company or a unit of an equity oriented fund is exempt under Section 10(38) of the Act. The objective of giving such exemption was that Indian residents should invest in the capital market for long term, however, by including such income in the book profit the benefit is taken back from the Companies. Taking back such benefit from the companies is not equitable.
- An eligible assessee can claim deduction under section 32AC of the Act while computing income under the normal provisions of the Act. However, presently, the assessee may have to pay MAT on the same though being eligible for the deduction under normal provisions of the Act diluting the benefit intended to be provided by the Government.
- As per section 115BBD of the Act, dividend paid by a foreign company to an Indian company, in which the Indian company holds 26% or more of the equity share capital in the foreign company, such dividends are subject to tax @ 15%. However, MAT is levied at a rate higher than 15% on such dividend income, which defeats the purpose for which section 115BBD was introduced. The consequence is that an Indian companies will end up paying an effective tax of 21.34% on foreign dividend due to applicability of MAT provisions as against the effective rate of 17.30% stipulated under the provisions of section 115BBD of the Act. Further, since the Indian companies have made outbound investments through investment companies which generally do not have any other source of income, the companies would not be able to utilize the MAT credit.
- The Finance Act, 2011 broadened the scope of MAT by bringing SEZ developers and

units under the ambit of MAT thereby significantly diluting benefits offered under the popular SEZ Scheme. In this regard, the Finance Minister in his Budget speech for 2014-15, stated that manufacturing is of paramount importance for the growth of the economy. He further stated that the Government is committed to revive the SEZs and make them effective instruments of industrial production, economic growth, export promotion and employment generation.

- Section 115JB(7) of the Act states that where the assessee is a unit located in an International Financial Service Centre ('IFSC') and derives income solely in convertible foreign exchange, a lower MAT rate of 9% shall apply as compared to the present MAT rate of 18.5%. The Memorandum to Finance Bill 2016 states that the MAT rate applicable to a unit located in an IFSC has been reduced to 9% in order to provide a competitive tax regime to the IFSC. It is believed that the current MAT rate does not make the Indian IFSC globally competitive.
- Exemption from AMT is provided to certain specified persons if the adjusted total income of such person does not exceed Rs. 20 lakhs. The limit of Rs. 20 lakhs is inadequate considering especially the huge amount of investments made by the businesses in relation to export of goods and services.
- MAT provisions have been amended vide Finance Act 2016 to state that MAT will not be applicable to foreign companies in the following circumstances:-
  - Where the foreign company is resident of a country with which India has entered into a tax treaty and such foreign company does not create a Permanent Establishment ('PE') in India as per such tax treaty.
  - Where the foreign company is resident of a country with which India has not entered into a tax treaty and such foreign company is not obliged to seek registration under the relevant provision of the Companies Act, 2013.

  For MAT purposes, book profit are required to be computed under the Corporate Law. As per Corporate Law, an entity having a place of business in India (including in an electronic form) is required to maintain books of account. In light of the above, applicability of MAT to entities following gross or net basis of taxation would depend on its presence or place of business in India.

  Based on presumptive tax regime (e.g.; taxability under section 44BB of the Act), companies opting for deemed taxation under the said section are not required to maintain books of accounts for the purposes of the Act. However, as stated above, for MAT purposes, book profit is required to be computed under the Corporate Law.

  There is an ambiguity whether companies taxed under presumptive tax regime and are provided with specific exemption from maintaining book of accounts under the Act, would be eligible to MAT provisions.
- The Finance Act, 2017 made certain amendments to section 115JB of the Act to provide the framework for computation of book profit for Ind AS compliant companies in the year of adoption and thereafter. The issues emanating therefrom are given below for

the consideration of the Government:-

- In section 115JB(2A) of the Act, no exceptions are provided for capital items which are not subject to tax at all. If no exceptions are provided then any capital items such as equity component of Compulsory Convertible Preference Shares ('CCPs'), Compulsory Convertible Debentures ('CCDs') etc. would also get taxed without getting a corresponding deduction. Credit adjustments of ESOP reserve would also get taxed. ESOP reserve is not income per se but only corresponding entry for ESOP expenditure. If the amount of reserve created is taxed, companies will not be able to claim deduction for ESOP expenditure. Items which are capital in nature and not chargeable to tax, would get taxed. It may also be clarified that transition amount should exclude ESOP reserve/equity component of CCPs or CCDs which has been reclassified/created on transition from Indian GAAP to Ind AS. It is suggested that section 115JB(2A) of the Act may be amended to provide that the book profit as computed in accordance with Explanation 1 to subsection (2) to section 115JB of the Act shall be further increased/decreased by all amounts or aggregate of the amounts credited/debited during the previous year to any item of other equity, as the case may be, but not including certain items.

- Under Ind AS, prior period adjustments are not reflected in the financials in which error is discovered but earlier period financials are restated to which such errors pertain. There is no clarity on how book profit would be adjusted if the return of income for that year has already been filed and due date of filing revised return has lapsed. Specific provision for revising return in the above situation may be provided or prior period adjustments may be allowed to be adjusted from book profit in the year in which errors are discovered.

- CBDT circular no 24/2017 dated 25 July 2017 clarifies that adjustments relating to provision for doubtful debts shall not be considered for the purpose of computation of the transition amount. There is no clarity on whether reversal of provision for doubtful debts should also be excluded in computing the book profit for MAT purposes in subsequent years. As per provisions of clause (i) of Explanation 1 to section 115JB of the Act, any amount withdrawn from any provision should not form part of the book profit for MAT purposes, provided that such provision amount was added to compute the book profit of the year in which the provision was created. On plain reading of the proviso to clause (i) to Explanation 1 to section 115JB, it is clear that unless the book profit has been increased in the year in which provision was made for MAT purposes, the reversal of such provision subsequently cannot be reduced in computing book profit. A difficulty which arises is that the reversal of provision for expected credit loss may not be reduced in computing book profit as such provision was not added back in the year the provision was created. It is suggested that it may be clarified that the reversal of provision made for expected credit loss for the period prior to convergence year not forming part of transition amount should not form part of the book profit in the subsequent years when such provision is reversed.

- As per clause (f) of Explanation 1 to Section 115JB of the Act, expenditure relatable to exempt income which is debited to the profit and loss account needs to be added back for the purpose of computation of book profit under Section 115JB of the Act. However, it has been observed that the deeming provisions of Section 14A of the Act read with Rule 8D of the Income Tax Rules, 1962 ('the Rules') are applied by the tax officers to disallow the expenditure incurred in relation to exempt income for the purpose of computing the book profit under Section 115JB of the Act. The law is settled today that only adjustments as provided in Explanation 1 to section 115JB of the Act are allowed to determine the book profit for the purpose of MAT. The practice adopted by the tax officers in disallowing expenditure as per deeming provisions of section 14A read with Rule 8D of the Rules is against the provisions of Section 115JB of the Act and result into disallowance of expenditure in excess of the expenditure actually incurred and debited to the profit and loss account.
- The tax on perquisite borne by the employer is wrongly being interpreted as 'income tax' by the tax officers in some cases for the purposes of adjustment to book profit as provided under Explanation 1 to section 115JB of the Act. It is emphasized that tax on perquisite is being paid by the employer on behalf of employee and does not fall within the purview of 'income tax' for the purposes of section 115JB of the Act.

Recommendations

- With the phasing out of exemptions and deductions available under the Act, the burden of MAT should also be gradually reduced from the current levels of 18.5 per cent to a rate which will be commensurate with the phasing out of tax exemptions and incentives.
- It is submitted that relief from MAT should also be granted to cases covered by IBC provided the Resolution Plan is approved by the National Company Law Tribunal. This will provide an additional fillip to entities to approach the Insolvency & Bankruptcy Board and will go a long way in achieving the objects of IBC and in reviving the distressed sector. Companies should be allowed to set-off entire past book losses including unabsorbed depreciation before they are subjected to MAT. Further, the methodology for computing loss brought forward and unabsorbed depreciation as per books of account be specifically provided in section 115JB of the Act.
- The MAT/AMT credit should be allowed to be carried forward and set-off without any time limit.
- Currently, sale of listed securities is free from levy of Capital Gains Tax. This has resulted in buoyancy of Capital Markets, promoted substantial FII inflows and ensured transparency. However, there is one lacuna here. If the seller of the listed shares is a company, there is no taxability of the gains but the book profit are subject to the levy of Minimum Alternate Tax (MAT). The levy of MAT at 20 per cent + defeats the very exemption from levy of capital gains tax. It is therefore suggested that profits which are exempt from levy of capital gains tax be also not taken as part of book profit for the purposes of MAT.

- The investment allowance @ 15% eligible for deduction under section 32AC of the Act should be reduced while computing book profit of the company under the provisions of section 115JB of the Act.
- It is recommended that dividend received from foreign company should be exempt from MAT just like domestic dividend is exempt from MAT.
- MAT on SEZ developers and units should be abolished.
- MAT should be abolished for a unit located in an IFSC to compete with tax breaks offered by IFSCs globally (e.g. Dubai (0%), Malaysia (3%).
- The threshold limit from exemption of AMT should be increased from Rs. 20 lakhs to Rs. 50 lakhs.
- The amount of weighted deduction under Section 35(2AB) of the Act should be deducted while computing MAT. The benefit of investment linked deductions is getting diluted as MAT/AMT at 18.5% applies on book profit. Therefore, these deductions should also be allowed while computing the book profit/adjusted total income under the provisions of Section 115JB/Section 115JC of the Act respectively.
- In computing the adjusted total income for AMT, investment linked deductions on capital expenditure for specified business (net of depreciation) should not be added back under Section 115JC of the Act.
- To attract more industrial and infrastructural investments, MAT/AMT on eligible businesses/industrial undertaking should be abolished.
- Set off of MAT credit should be allowed in full (including applicable surcharge and cess paid on MAT).
- It should be clarified that MAT provisions would not apply to foreign companies which are taxed as per the provisions of presumptive tax regime under the Act.
- A specific clarification should be issued to provide that the provisions of Section 14A of the Act read with Rule 8D of the Rules cannot be applied for the purpose of computation of disallowance of expenditure under clause (f) to Explanation 1 to Section 115JB of the Act. It further needs to be clarified that it is only the actual expenditure incurred to earn exempt income and debited to the profit and loss account which has to be added to compute the book profit under Section 115JB of the Act.
- It should be clarified that tax on perquisite borne by the employer on behalf of the employee is not to be considered as income-tax for the purpose of adjustments required as per Explanation 1 to section 115JB of the Act.

4.4. Tax Rate for transactions done through mode other cash

Issue

In case of presumptive taxation regime under section 44AD of the Act it has been provided that lower rate of 6% would apply instead of 8% for receipts through account payee cheque drawn on bank or account payee draft or use of electronic clearing system through a bank

account. The intent appears to be conceptually a push for digital transactions; however, there are certain digital modes of payment like mobile wallets, credit cards etc., which may still be not covered within the scope of the defined mode of payment (as they only cover transactions done by electronic clearing system through a bank account).

Recommendation

In all the sections introduced to promote digital economy, the mode of payment should be defined in such a manner that all non-cash transactions done through traceable mode should be covered within the ambit.

It is further suggested that benefit of lower rate of tax @ 6%, should also be extended for presumptive tax under section 44ADA (presumptive tax for professionals) and 44AE (presumptive tax for truck owners).

4.5. Dividend Distribution Tax - Section 115-O

Issues

- As per the provisions of Section 115-O of the Act, the domestic holding company will not have to pay DDT on dividends paid to its shareholders to the extent it received dividends from its subsidiary company on which DDT has been paid by the subsidiary. However, the provision as it stands on today, gives relief in respect of dividend received from only those companies in which the recipient companies are holding more than half of the nominal value of equity capital. The condition that the dividend should be received from a subsidiary is in a sense restrictive, as a company is stipulated to be a subsidiary of another company, if such other company, holds more than half in nominal value of the equity share capital of the company. The said condition is unlikely to be fulfilled by majority of the promoter companies which hold investment in operating companies listed on stock exchanges. Even shareholders of joint venture companies are impacted by the above restrictions. In both the scenarios, since the operating/joint venture company i.e. the company declaring the dividend is not a subsidiary of any company, the first condition i.e. dividend should be received from a subsidiary company is never fulfilled and accordingly when the promoter company/shareholder of joint venture company declares dividend to their shareholders, it cannot deduct the dividend so received from the operating/joint venture company for the purpose of payment of DDT.
- The proviso to Section 115-O(1A) of the Act provides that the same amount of dividend shall not be taken into account for reduction more than once. The levy of Dividend Distribution Tax (DDT) at multiple levels has been a subject matter of grievance by corporates. A part of this issue has been resolved by providing in the Act that if a holding company receives dividend from its subsidiary, a further distribution of dividend by the parent will not attract levy of DDT. However, proviso to section 115-O(1A) of the Act raises ambiguity regarding the cascading effect of DDT in a multi-tier structure which is against the intent of the Government. Further, as it happens, promoter holdings in operating companies are not necessarily in a single parent. Also, irrespective of whether there exists a parent-subsidiary relationship, a tax on dividends which have already suffered levy of DDT amounts to multiple taxation and needs to be avoided.

- Further, the Finance Act, 2011 has also burdened the SEZ developers by including them in the scope of DDT.
- The earlier DDT rate of 10% was lower in line with the rate of TDS on dividends in most Indian and international tax treaties. The increased basic DDT rate of 15% (effective rate of about 20%) reduces the dividend distribution ability of domestic companies and the uncertainty with respect to its credit in overseas jurisdictions impacts the non-resident shareholders adversely.
- Currently, DDT is also levied on undertakings engaged in infrastructure development which are eligible for tax benefit under Section 80-IA of the Act. This is detrimental to the growth of infrastructural facility in India.

Recommendations

- All dividends on which DDT has been paid, be allowed to be reduced from dividends irrespective of the percentage of equity holding keeping in mind that investment companies which do not necessarily own/have subsidiaries as they invest in various companies in the open market, be also made eligible for such benefit. Thus, irrespective of whether there exists a parent-subsidiary relationship, a tax on dividends which have already suffered levy of DDT amounts to multiple taxation and should be avoided.
- It is suggested that dividends which have suffered DDT be treated as pass through and be not subjected to levy of DDT. It is recommended that an appropriate explanation be inserted clarifying that the benefit of DDT paid by a subsidiary company is available at each company level in a multi-tier corporate structure so as to avoid the cascading impact of DDT. This will go a long way in boosting investor's confidence and improve the ease of doing business in India.
- To attract more investment in the SEZs, DDT on SEZ developers and units should be abolished.
- The tax rate of DDT is recommended to be reduced to 10% from the current effective rate of about 20% (after including the education cess, surcharge and grossing-up of the dividend).
- To incentivise the investment in infrastructure sector, it is recommended that DDT on industrial undertakings or enterprises engaged in infrastructure development, eligible for deduction under Section 80-IA of the Act or section 35AD of the Act, should be abolished.

4.6. Tax on certain Dividends received from Domestic Companies - Section 115BBDA

Issue

The insertion of section 115BBDA in the Act to tax dividends in the hands of the recipient which have already suffered corporate tax, dividend distribution tax; results in economic triple taxation.

Recommendation

It is recommended that new levy amounting to third level of taxation on profits may be done away with. Alternatively, tax paid by the company under section 115-O of the Act should be allowed as a credit against the tax payable by the shareholder.

4.7. Deemed Dividend - Section 2(22)(e)

Section 2(22) of the Act defines the term 'dividend' and sub-clause (e) thereof includes, within the meaning of this term, even an advance or loan, to a shareholder having at least a 10% voting-power in a company in which the public are not substantially interested, to the extent that the company possesses accumulated profits. Thus, a payment, which is clearly not a dividend as commercially understood, is, by a fiction of law, deemed to be one. Apart from payment to the shareholder himself, a loan or advance to any concern in which he is a partner or a member, with a beneficial interest of not less than 20% is also considered, to be deemed dividend, and is taxed accordingly. The object clearly is to prevent tax-avoidance by deeming an advance or loan (which would not be taxable) as dividends which is subject to income tax.

4.7.1. Taxability of Genuine Inter-corporate Loans and Advances as Deemed Dividend

Issues

The provision suffers from many inequities:-

- It taxes a loan, though it may be quite a genuine one (e.g. advance for purchase of goods/services), which is duly repaid within its scheduled short time. There are genuine cases where funds may be required at the shareholder level for a shorter duration, and the amount is actually repaid within the same year. Currently, in absence of any exception, in such cases, it creates compulsion on the shareholder to borrow from outside sources. Moreover, there is no corresponding tax-relieving provision at the time of recovery of the loan.
- The tax is attracted, notwithstanding that the loan may be advanced at a fair commercial rate of interest and notwithstanding that preponderant majority of persons owning the concern which received the loan are not even shareholders of the lending company.
- It creates hindrances for cash pooling arrangements and common treasury management functions between group companies and impacts ‘ease of doing business’ for taxpayers.

Recommendations

- Levy of tax on deemed dividend in the hands of shareholder at the normal rate is unjustifiable especially when all other deemed dividends are also subjected to DDT. If this suggestion is not accepted, then adequate provisions should be made to exclude genuine transactions from the consequences of these provisions.
- Illustratively, genuine loans and advances, given on current market rate of interest and which are re-paid during the year, should be excluded from the scope of deemed

dividend as these are not a subterfuge for payment of dividend.

- Loan given as part of business transaction and Inter-corporate deposits should specifically be excluded from the application of section 2(22)(e) of the Act to avoid unnecessary litigation.

4.7.2. Accumulated Profits not to include Capital Reserves - Section 2(22)(e)

Issue

- As per the Companies Act, capital reserves cannot be utilized for distribution of dividend by a company. This leads to controversies as to whether capital reserves should form part of accumulated reserves for the purpose of Section 2(22)(e) of the Act.

Recommendation

- An amendment should be brought in Section 2(22) of the Act to exclude capital reserves from the ambit of "accumulated profits".

4.7.3. Taxability of Deemed Dividend in the hands of Recipient not being a Shareholder

Recommendation

- The object of sub-clause (e) of Section 2(22) of the Act is to prevent tax-avoidance by making an advance or loan (which would not be taxable), as a deemed dividend to the shareholder, which is subject to income tax. It is recommended that the threshold for substantial interest of the shareholder in the recipient concern should be increased to 51%.

4.8. Phasing out of Deductions and Exemptions vis-à-vis industry needs

Some of the recommendations in relation to phasing of following profit linked incentives and weighted deduction by amendments in the Act are as below:-

- There are various sectors (capital intensive; pharma; long term projects like SEZ's; etc.) where the turnaround time for the companies/products to reach a break even and start earning profits takes longer than some other industries. Some of the sectors would take long for the completion of projects for example deduction under Section 80-IA(4) of the Act dealing with development, operation and maintenance of an infrastructure facility, deduction under Section 80-IAB of the Act dealing with development of special economic zone, deduction under Section 80-IB(9) of the Act dealing with production of mineral oil and natural gas, etc. Further, the phasing out of incentives/exemptions is also likely to impact the government's agenda of 'Make in India', 'Digital India' etc.
- The provisions of MAT were introduced as a result of certain deductions and exemptions available to the taxpayers under the Act. While introducing MAT provisions, it was mentioned in the memorandum explaining the provisions of the Finance Bill 1987 that certain companies making huge profits were managing their affairs in such a way as to avoid payment of income tax. Basic purpose of introducing MAT was to bring all zero tax companies within the tax net. It was introduced to neutralize the impact of incentives.

However, with phasing of incentives and deductions under the Act, the rate of MAT has not been reduced.

Recommendation

- The government and health care sectors as well have long gestation periods. There would be certain entities which would have recently commenced commercial operations, and will have to tackle phasing out much faster than anticipated and planned. This would have an adverse impact on the commercial viability as well as the profitability of the said entities. The doing away of weighted deductions could also impede the innovation process in case of certain sectors for e.g. the pharma, etc. and is likely to impact the government's 'Make in India' campaign. The process of phasing out of exemptions and deductions should not be done across sectors. Further the weighted deduction needs to be reinstated in case where it has been withdrawn. Thus, the phase out of deductions and exemptions should be applicable to select sectors based on long-term plans of the government to nurture the growth potential sectors considering a sensitivity analysis of the said sectors.
- It is recommended that with phasing out of incentives, the Government should consider reducing the burden of MAT on the taxpayers and MAT should eventually be phased out.

4.9. Income Computation and Disclosure Standards ('ICDS')

On 31 March 2015, the Government had issued 10 Income Computation and Disclosure Standards (ICDS), operationalising a new framework for computation of taxable income by all assessees in relation to their income under the heads 'Profit and gains of business or profession' and 'Income from other sources'. These standards were to be applicable for Previous Year (PY) commencing from 1 April 2015, i.e., Assessment Year (AY) 2016-17 onwards. Based on various representations made by the stakeholders at large, the Expert Committee was constituted to examine stakeholder's representations and the Committee recommended for amendments to be made to the notified ICDS as well as issuance of clarifications in respect of certain points raised by the stakeholders. The Government vide Press release dated July 6, 2016 announced revision of ICDS and deferment of ICDS for one year and to be applicable from April 1, 2016 instead of April 1, 2015. The CBDT through its notification no. 87/2016 dated September 29, 2016 has notified revised ICDS (to be applicable from A.Y.2017-18) and repealed its earlier notification no. 32/2015 dated March 31, 2015.

Issues

- It is observed that there is no international precedent on ICDS. ICDS at best leads to timing difference between accounting and taxable income.
- Taxpayers are already grappling with multiple regulatory changes like Companies Act, Ind-AS and GST. There is also scope for litigation on many aspects of ICDS. Further, ICDS merely results in multiplicity of accounting methods, increased compliance burden of multiple records, etc. which outweigh the benefits to be gained by application of ICDS.

- ICDS has deviated from recognised accounting principles viz. materiality and prudence. It alters the settled legal positions and will add to enormous litigation.
- The revised ICDS were notified by the Government on September 29, 2016 leaving no time for the taxpayers to analyse the impact of the same.

Recommendation

It is recommended that ICDS should be withdrawn or at least provisions of ICDS should be deferred for a reasonable period of time.

4.10. Place of Effective Management

The Finance Act, 2015 has modified the condition of determining residential status of a company. A company will now be resident in India if it is an Indian company; or its place of effective management in that year, is in India. Place of effective management ('POEM') means a place where the key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance made. The Finance Act 2016 deferred the provisions of Place of Effective Management (POEM) by 1 year i.e. to be effective from Financial Year (FY) 2016-17. The final guiding principles for determination of POEM were issued by CBDT vide Circular No. 6 dated January 24, 2017, almost before the end of the financial year 2016-2017. It is believed that very little time was left with the taxpayers to study and analyse the impact of these guidelines. Further, some of the issues with regard to these guidelines still remain unaddressed.

Further, a new chapter XII-BC consisting of section 115JH was inserted into the Act vide Finance Act, 2016 with effect from AY 2017-2018. The section inter-alia provides that where a foreign company is a resident in India during any previous year (being the first year) by virtue of section 6(3) of the Act, the provisions of the Act relating to computation of total income, treatment of unabsorbed depreciation, set off or carry forward and set off of losses, collection and recovery, and special provisions relating to avoidance of tax shall apply for that year with such exceptions, modifications and adaptations, as may be notified. The draft notification under section 115JH of the Act for implementation of POEM was issued by the Government on June 15, 2017 applicable from AY 2017-2018, inviting comments by 23 June 2017. FICCI has made detailed suggestions in regard to the draft notification. However, the final rules in this regard are yet to be notified. This leaves very little time for the taxpayers to understand and apply the transition provisions considering the fact that the due date for filing the tax return is 30 November 2017.

In the above background and in the absence of the road map for implementation of POEM, it is recommended that the applicability of POEM be deferred to FY 2018-19 (AY 2019-20).

As mentioned above, inspite of the above guiding principles and the draft notification, issues which still remain unaddressed are given below for kind consideration of the Government:-

4.10.1. Definition of Items of Passive Income

The CBDT vide circular no 6 of 2017 dated January 24, 2017 has notified the final guidelines for determination of POEM of a foreign company in India. As per the said circular, 'active

business test' has been specified for determination of POEM. The circular provides that a foreign company would be engaged in active business outside India if its passive income is not more than 50 % of its total income. The term 'passive income' has been defined as under:

'Passive income of a company shall be aggregate of, -

(i) income from the transactions where both the purchase and sale of goods is from / to its associated enterprises; and

(ii) income by way of royalty, dividend, capital gains, interest or rental income;

The final guidelines have clarified that income by way of interest shall not be considered passive income in case of a regulated company engaged in the business of banking or a public financial institution. It is however emphasised that a particular stream of income can be the core business income for some companies while for others it may be arising from non-core business activities of the company. The guidelines does not make any distinction whether the business of the company is to generate income from such stream or not. By virtue of passive income criteria, software companies, e-commerce companies, telecommunication companies or for that matter any other technology company which though engaged in an active line of business would be considered to be earning royalty income instead of business income and hence, will never be able to satisfy the test to be considered as engaged in an active business. It is recommended that income earned by a foreign company from provision of services by using its assets like telecom network; software etc. should be specifically excluded from the scope of passive income especially in light of the retrospective amendment widening the scope of "royalty".

It is further suggested that "Passive income" should be clarified to mean any income earned from a passive activity i.e. an activity which is non-core activity for the company. Reference can be drawn to the financial statements where such non-core income is categorized as other income or extraordinary income and only such income should be brought within the purview passive income.

4.10.2. Use of average data of 3 years

The guidelines provide that for the purpose of determining whether the company is engaged in active business outside India, the average of the data of the previous year and two years prior to that shall be taken into. The guidelines provides that POEM would be required to be determined on a year to year basis. Since, determination of POEM is a yearly exercise the use of average of data of two prior years may not represent a correct picture of the conduct of business of a company. In this regard, reference is made to the following examples:

- A company may earn substantial capital gain from sale of investments in one of the years under consideration. While computing average it may also inflate the figure of passive income for the years when it generating only active income.

- A company may have more share of passive income when its main business may be facing recession in a year or may have lost a main customer in a year. Due to this, the figure of passive income for other years may inflate while computing average.

It is recommended that only the data of the previous year should be used for determining whether the company is engaged in active business outside India during the year or not.

4.11. 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.

Recommendations

- 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.

4.12. Equalisation Levy

The Finance Act, 2016 has introduced a new 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.

Specified services has been defined to mean online advertisement, any provision for digital advertising space or any other facility or service for the purpose of online advertisement and any other services notified by the Central Government.

Issues

- The Vienna Convention, which lays downs the fundamental principles for applicability of tax treaties, states that the tax treaties are binding on countries and must be honored in good faith. Since the equalization levy is essentially in the nature of a tax on income and hence, should ideally qualify within the meaning of the term 'taxes' under India's tax treaties, applicability of this levy in situations where the tax treaties provide taxing rights only to the country of residence (such as where the recipient earns business income and does not have a PE in India) goes against the fundamental principles of bilateral treaty negotiations. Levying income tax outside of Tax treaties overwrites the tax treaties unilaterally and will lead to double taxation.
- Foreign digital advertising companies operating in India through Indian establishments who act as reseller/distributor of digital ad space i.e. purchasing online ad space from offshore and selling to the advertisers in India. The Indian establishments pay income tax in relation to such digital advertisements. Indian establishments pay income tax on its profits which is determined in accordance with Income Tax/Transfer Pricing regulations in India. Once Indian establishment is paying income tax on its India activities, levying Equalisation levy on payment for purchase of online Ad space is clearly levying additional income tax on the same income. Exemption from this levy has been granted to Permanent Establishments (PE) because PE will be paying income tax based on activities performed in India. Similarly Indian establishments acting as a reseller/distributor of digital advertisement space is paying income tax based on activities performed in India.
- The equalization levy at the rate of 6 percent on gross consideration received or receivable by a non-resident (in the absence of a PE) is too high. An equalization levy of

6 percent on gross basis would mean a profit attribution of around 47 percent[1] to Indian activities (considering a profit margin of 30 percent and tax rate of 43.26 percent), which is an unreasonably high amount of attribution to India, considering the fact that the only nexus with India is on account of the fact that the customers are located in India. The actual income-generating activities of the non-resident are the technology/product and functioning of the same on the data centers/ servers/ other infrastructure on a real-time basis, which are all carried out outside India.

- The equalization levy is not chargeable in cases where the non-resident service provider has a PE in India. However, it could be possible that the payers would have deducted equalization levy on the understanding that the non-resident does not have a PE in India (as required under the equalization levy chapter) and subsequently, the Indian tax authorities allege a PE of the non-resident and demand income-tax under the Act on the income attributable to the PE. In such cases, since equalization levy does not form part of the Act, credit for such levy may not be available against the income tax demand raised by the Indian tax authorities under the Act. This could potentially lead to double taxation of income in the hands of the non-resident service provider.
- The levy is applicable in case of payments made by a person resident in India carrying on business, irrespective of whether the payments are made for carrying on a business in India or outside India. The scope of the levy appears to include payments made by resident for overseas business activities. The applicability of the levy could be viewed as 'extraterritorial' and could lead to protracted litigation.
- 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.
- There is no clarity on the applicability of the levy on cross charge received by Indian entities from their overseas parent for various group services.
- There is also no clarity on applicability of the levy on payment made by a branch of an Indian entity based outside India to a non-resident and also as to whether surcharge and education cess would be further applied on equalisation levy of 6%.
- There is no specific provision for filing appeal against intimation of processing of annual statement of equalization levy.

[1]Assume an advertiser in India makes a payment of INR 100 towards online advertisement to non-resident foreign company:

Equalization levy @ 6 percent on consideration (INR 100) = [100*30 percent (Profitability)] X [47 percent attribution to India] X [43.26 percent tax rate on foreign companies]

- Lastly, the trend of India levying additional tax (such as the Dividend Distribution Tax, the Buyback Tax and now the Equalisation levy) on Indian nationals significantly adds to the tax burdens on Indian businesses.

Recommendations

- There is a need to take a re-look on the validity of the Equalisation levy.
- Exemption from the levy should be granted to Indian establishments of non-resident digital companies who distribute online ad space in India to avoid double taxation in India.
- The levy should be introduced though a separate provision in the Act to address the issue of resultant double taxation in the hands of the Foreign Service provider due to non-availability of its credit in the foreign jurisdiction. This would enable a non-resident service provider to claim credit of Equalisation Levy paid in India against corporate Income-tax to be paid in the country of residence of such non-resident, subject to the domestic law provisions of the non-resident country. As an alternative, section 90(2) of the Act should be made applicable to Chapter VIII, which will allow the non-resident to claim beneficial provisions of the tax treaty.
- 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.
- The rate of levy should be brought down to 1% on gross basis due to wafer thin margins and since the digital ecosystem players are primarily being start-up companies facing losses in initial years.
- 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, advance payments, cross charge scenario, applicability of levy on payment by branch of an Indian entity based outside India, applicability of surcharge and cess on the levy etc. be clarified by the Government.
- The levy should not be made applicable to payments in respect of services utilized for carrying the business or profession outside India.
- Specific provision be introduced for appeal to be made against intimation of processing of annual statement of equalization levy.

4.13. Rationalization of provisions of Section 14A and Rule 8D

As per Section 14A of the Act, no deduction shall be allowed in respect of expenditure incurred in relation to income not includible in the total income. Section 14A(2) of the Act provides that the amount of expenditure incurred in relation to income not includible in the total income shall be determined by the tax officer if he is not satisfied with the correctness of the claim of the taxpayer in respect of such expenditure in relation to income not includible in the total income. This satisfaction is to be arrived at by the tax officer having regard to the accounts of the taxpayer. The determination of the amount of expenditure incurred in relation to the income which is not includible in the total income of the taxpayer is to be done in accordance with the method prescribed, i.e. Rule 8D of the Rules. There has been a spate of litigation on the application of the section, illustratively, with respect to issues related to the quantification of the amount of expenditure attributable to exempt income, identification of exempt income.

Issues

- In pursuance of recommendation by Income Tax Simplification Committee, the CBDT vide Notification No. 43/ 2016 dated June 02, 2016 partially substituted existing Rule 8D for computing disallowance of expenditure incurred in relation to exempt income. The modified Rule provides for a new method for computation of disallowance of expenditure which, in addition to amount of expenditure directly relating to exempt income, shall include an amount equal to 1% of the annual average of the monthly average of the opening and closing balances of the value of investment which gives rise or may give rise to exempt income. Rule 8D further provides that the total amount of disallowance shall be restricted to total expenditure claimed by taxpayer. However, it has been noticed that even if exempt income is not earned during a particular year, the tax officers disallow the expenditure in relation to the investments which have the potential to earn tax exempt income.
- Ind-AS 109 provides that the Companies need to carry investment in equity shares (other than investment in Subsidiary, Associates and JV) at Fair Market Value. Also the Company may opt to revalue its investments in Subsidiary, Associates and Joint Venture at fair market value as per the option provided under Ind-AS 101. This exercise will lead to notional increase/decrease in the value of investment. Since computation of disallowance under section 14A of the Act read with Rule 8D of the Rules includes an amount equal to 1% of the annual average of the monthly average of the opening and closing balances of the value of investment. It should be clarified that disallowance on account of section 14A of the Act has to be computed based on actual cost of investment to avoid any probable litigation on this account.
- As per clause (f) of Explanation 1 to Section 115JB of the Act, expenditure relatable to exempt income which is debited to the profit and loss account needs to be added back for the purpose of computation of book profit under Section 115JB of the Act. However, it has been observed that the deeming provisions of Section 14A of the Act read with Rule 8D of the Rules are applied by the tax officers to disallow the expenditure incurred in relation to exempt income for the purpose of computing the book profit under

section 115JB of the Act. It has been even held by the Supreme Court that only adjustments as provided in Explanation 1 to section 115JB of the Act are allowed to determine the book profit for the purpose of MAT. The practice adopted by the tax officers is against the provisions of Section 115JB of the Act and result into disallowance of expenditure in excess of the expenditure actually incurred and debited to the profit and loss account.

- Further, dividend which is subject to DDT and share of profit from partnership firm which has been subject to tax in the hands of partnership firm should not be treated as exempt income and corresponding expenditure should not be disallowed under section 14A of the Act.

Recommendations

- It should be explicitly clarified that disallowance under section 14A of the Act should not be triggered if no income which does not form part of the total income under the Act has been earned in a particular year.
- It should be clarified that disallowance on account of section 14A of the Act has to be computed based on actual cost of investment.
- A specific clarification should be issued to provide that the provisions of Section 14A of the Act read with Rule 8D of the Rules cannot be applied for the purpose of computation of disallowance of expenditure under clause (f) to Explanation 1 to Section 115JB of the Act. It further needs to be clarified that it is only the actual expenditure incurred to earn exempt income and debited to the profit and loss account which has to be added to compute the book profit under Section 115JB of the Act.
- Share of profit from partnership firm in the hands of partner, Dividend income in hands of shareholders, income arising to shareholder on account of buy-back of shares, income arising to a unit holder in respect of units of a Mutual Fund, specified undertaking, specified company, distributed income referred to in section 115TA of the Act received from securitisation trust by any person being an investor of the said trust and which has been already subject to tax should not be treated as exempt income and corresponding expenditure should not be disallowed under section 14A of the Act.

4.13.1. Tax on income from transfer of carbon credits – Section 115BBG

The controversy surrounding the taxation of income from the transfer of carbon credits has been going on for a while now. Introduction of section 115BBG to the Act providing for a 10% tax on income from transfer of carbon credits is a very welcome move. However, since the amendment is a prospective one, litigation for assessment years prior to AY 2018-19 may continue to fester. This coupled with the fact that the global market for carbon credits has all but collapsed and alternative bilateral offset mechanisms are being explored leads to unnecessary hardship for taxpayers.

It is suggested to extend the benefit of this 10% rate to earlier years also as it will go a long way towards furthering the Government's stated objective of curbing litigation as also supporting projects that have helped the global environment by reducing carbon emissions.

To this end, for the periods prior to Assessment Year 2018-19, we submit that an option may be given to taxpayers to voluntarily offer income from transfer of carbon credits to tax at the same 10% rate as present in section 115BBG of the Act. This can help put an end to protracted litigation on the issue. Considering that such receipts have been held as non-taxable capital receipts by some High Courts, such a move will also benefit the exchequer.

An appropriate framework for this option (though a Scheme, Notification, Circular etc.) may be considered. This framework could, inter alia, provide that:

- The 10% tax rate is optional for taxpayers who wish to obtain finality on this issue without pursuing further appellate or judicial remedies.
- Such an option could be exercised by the taxpayer making a declaration with his jurisdictional Commissioner.
- Once such a declaration is scrutinised, no Tribunal or Court should proceed to decide any issue relating to taxation of income arising from transfer of carbon credits. In other words, all proceedings with respect to such issue should abate.
- No interest and penalty should be leviable on such taxes.

4.14. Issues related to allowability of certain Expenditures, Deductions and Disallowances

4.14.1. Depreciation – Section 32

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.
- 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. However, as per the announcement made by the Finance Bill, 2016, the highest rate of depreciation has now been restricted 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. is 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.

- Need for Higher depreciation for plant and machinery.
- 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'.

4.14.2. Deduction of ESOP Expenditure

Issue

ESOPs are granted to employees to reward/ remunerate them for their contribution to the organisation and to retain talent. SEBI guidelines prescribe charging of ESOP discount in the

books of accounts. This charge to P&L account has, however, been disallowed in majority of the cases by the assessing officers on the ground that it is capital expenditure, and is contingent in nature. This is contrary to SEBI guidelines and against the basic objective of an ESOP viz to motivate & keep employees committed to organisation.

Recommendation

- Specific provision be introduced in the Act for allowing ESOP Expenses. A separate section for such allowance is suggested which is in line with voluntary retirement scheme provisions dealt with under section 35DDA of the Act.

4.14.3. Tax treatment of 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 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.

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.

4.14.4. Allowability of Annual Contribution to an Approved Gratuity Fund by the Employer

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.

4.14.5. Disallowance - Section 40(a)

Issues

- The Finance Act (No 2), 2014 amended Section 40(a)(ia) of the Act to provide that if specified payments to residents are made without TDS, it will result in disallowance of only 30% of the such payments and the payer is considered as an assessee in default. Prior to FY 2014-15, entire amount (instead of 30%) of the specified payments on which tax was not deducted was disallowed under Section 40(a)(ia) of the Act. There is an interpretation issue that whether an expenditure which suffered 100% disallowance prior to this amendment for default in TDS in earlier financial year will now be allowed only to the extent of 30% in the year of payment of TDS on account of strict reading of proviso to section 40(a)(ia) of the Act.
- It has also been observed that in a case where there has been partial compliance with the tax withholding provisions (say, tax may have been withheld @2% as opposed to the correct rate of 10%), still, the disallowance is imposed with reference to the entirety of expenditure rather than on a proportionate basis. While there are certain decisions which have held that no disallowance can be made in case of short deduction of tax, the Kerala HC in the case of CIT v. PVS Memorial Hospital Ltd (380 ITR 284)(Ker) has taken a strict view that full disallowance will apply if there is short deduction. Hence, this issue requires clarity and resolution at the earliest to avoid further litigation.
- No disallowance shall be made and the taxpayer shall not be treated as an assessee in default, where the resident payee has paid the taxes due on such receipt and furnished evidence in support of this such as return of income for that year, a certificate from accountant to this effect etc. This benefit is only available in case of resident payees.

Recommendations

- It is recommended that the provisions of Section 40(a)(ia) should clarify that if, in earlier years, the disallowance of 100% was made, then 100% of the amount should be allowed as deduction on payment of such taxes to the Government Treasury during the subsequent years (instead of 30%).
- It is recommended that 30% disallowance should be restricted on the part of the payment on which the tax was not deducted/deposited at source and not of the entire payment.
- In order to align the two sub section (i) and (ia) of Section 40(a), it is also suggested that Section 40(a)(i) of the Act should be amended to provide the following:-

- 30% disallowance, instead of 100% disallowance for amount paid/payable to non-residents,
- no disallowance in cases where the due taxes have been paid by the non-resident payees subject to conditions as applicable in case of resident payees.

Issue

It has also been observed that the assessing officer during the course of the assessment proceedings disallow the expenditure under section 40(a)(ia) of the Act even in cases where the assessee has already been subject to TDS proceedings under section 201 of the Act and has not been treated as 'assessee in default' for failure to deduct or pay tax in accordance with the provisions of Chapter XVII of the Act. It is observed that if the assessee has been subject to detailed examination in respect of the compliances made by him under the provisions of Chapter XVII of the Act and no default is found by the TDS officer, then the assessee should not be subject to disallowance under section 40(a)(ia) of the Act.

Recommendation

It is recommended that suitable amendment should be made in section 40(a)(ia) of the Act to provide that no disallowance of expenditure will be made under this section for a previous year in which the assessee is not treated as an assessee in default as per the order passed by the TDS officer under section 201 of the Act .

4.14.6. Disallowance of Expenses incurred in favour of Members [Section 40(ba)]

Issue

Section 40(ba) of the Act does not permit deduction in the hands of AOP of any interest, salary, bonus, commission or remuneration paid to member of AOP. In many cases, a consortium may be formed by two or more members to jointly bid for big projects wherein each of the members brings in his own expertise and resources. If the consortium is assessed as AOP, the AOP's profits are assessed at higher amount by disregarding the commercial understanding between the parties for sharing of profits after factoring in specialised services or expert knowledge made available by some of its members. This results in disproportionate sharing of tax burden between the members. Unlike section 40(ba), section 40(b) permits deduction for interest and remuneration paid to partners of firm/LLP as per partnership agreement up to specified limits. This enables the partners to share the tax burden proportionate to their contribution to the firm.

Recommendation

To provide level playing field between firms and AOPs, an amendment may be made in the Act to provide for non-application of section 40(ba) for payments towards specialized services [i.e. expert knowledge] rendered by consortium members subject to the condition that deduction of payments made by consortium to its members will be allowed only if the same has been considered as income by the members in their respective return.

4.14.7. Disallowance under section 40A(3)

Issues

- Section 40A(3) of the Act disallows deduction in respect of any expenditure if payment

exceeding ten thousand rupees in a single day is made otherwise than by an account payee cheque drawn on a bank or account payee draft or use of electronic clearing system through a bank account. The intent appears to be conceptually a push for digital transactions; however, there are certain digital modes of payment like mobile wallets, etc., which are still not covered within the scope of the defined mode of payment (as they only cover transactions done by electronic clearing system through a bank account).

- Section 40A(3) of the Act does not restrict itself to transactions in Indian rupee but also covers cash payment in foreign currency. Companies do send their employees on business trips or for short duration assignments outside India or for supervising overseas projects. Incurring expenditure in case in excess of Rs. 20,000 outside India could be on account of the following:
    - High cost of living
    - Non-acceptance of travel cards/ credit cards at many places

The intention is not to evade taxes or carry out transactions in cash, it is only due to unavoidable circumstances that expenditure is required to be incurred in cash outside India. Triggering disallowance under section 40A(3) of the Act in such cases will lead to undue hardships to the taxpayers who have operations outside India.

Recommendation

- The mode of payment should be defined in such a manner that all non-cash transactions done through traceable mode should be covered within the ambit.
- Relaxation may be provided in Rule 6DD of the Rules where cash exceeding Rs. 20,000 is used in foreign country by employees on behalf of the company having regard to various factors such as high cost of living, non-acceptance of card, etc.

4.14.8. Deduction of Employees' Contribution to Provident Fund etc. – Section 43B

Issues

- Section 43B of the Act allows deduction towards employer contribution to PF/any other fund for the welfare of the employees if the same is deposited up to the date of filing the return of income. However, deduction for employees' contribution to PF/ESI or any other fund is governed by Section 36(1)(va) of the Act which mandates that the employees contribution should be credited to the relevant fund by the due date specified under the relevant Act, rule, order or notification governing that fund. Differential tax treatment for employees' contribution and employer contribution to the same fund is discriminatory and has led to unwarranted litigation.
- Section 43B of the Act provides that outstanding interest which is converted into loan shall be allowed as deduction as and when converted loan is repaid. This leaves ambiguity for interest which is converted into equity share capital of borrower at the option of the lender since equity share capital is not repaid in ordinary course of business. Hence, there is a risk that the taxpayer may lose deduction of such interest in

perpetuity.

Recommendations

- It is therefore recommended that suitable amendment be made in the Act so as to bring the provisions relating to the Employees' contribution towards employee welfare funds in line with the employer's contribution towards such funds.
- It should be clarified that where interest payable is converted into any type of share capital, the same would amount to actual payment of interest for the purposes of section 43B of the Act.

4.14.9. Exchange differences on Money borrowed in Foreign Currency

Issue

Section 43A of the Act allows an assessee to make adjustment in "actual cost" of the asset after the acquisition of assets from a country outside India on account of exchange rate fluctuation arising either on liability payable towards such foreign asset or on account of money repayable in foreign currency utilized for acquiring such foreign asset. The adjusted "actual cost" becomes the base for claiming depreciation. The provisions of section 43A of the Act does not specifically provide for such adjustment where the asset is acquired in India out of funds borrowed in foreign currency.

Recommendation

It is recommended that provisions of section 43A of the Act should be extended to allow for adjustment of foreign exchange fluctuation in "actual cost" even where the asset is acquired in India from foreign currency. This will not only bring parity between assets acquired from outside India and assets acquired within India but will also be in line with "Make in India" initiative of the Government. Alternatively, it is recommended that amendment be made in Section 43(1) of the Act to specifically provide for adjustment in "actual cost" on account of exchange difference on loan obtained from outside India but utilized to acquire assets in India.

4.15. General Anti Avoidance Rule - Chapter X-A

4.15.1. GAAR in the context of Treaty Override

The provisions of section 90(2A) of the Act reads as under:-

> "(2A) notwithstanding anything contained in sub-section (2), the provisions of Chapter X-A of the Act shall apply to the assessee, even if such provisions are not beneficial to him"

Issues

It is apparent from the above provision that the domestic tax law expressly provides that GAAR provisions may result in tax treaty override.

Insertion of this provision would go against the international principle on 'treaty overriding domestic tax laws'. A tax treaty is a bilateral agreement entered between two sovereign governments. As per Article 26 and 31 of the Vienna Convention, a tax treaty should be

implemented in good faith. Further as per Article 27 of the Vienna Convention, a government cannot invoke its internal law as a justification for its failure to perform the tax treaty. Therefore, a unilateral amendment in the domestic law of any particular country cannot override a tax treaty which has been signed with full knowledge, understanding and consent of both of the governments. 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 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 Limitation of Benefit ('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.

Recommendations

- Given the resultant implications on the non-resident taxpayers and the same being against the internationally accepted principles, it is suggested that sub-section (2A) of Section 90 of the Act should be withdrawn.
- Without prejudice to the above, 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 the Principal purposes of transactions provisions) dealt with by the tax treaty between India and the respective country, the same should not be further subjected to GAAR provisions. It is submitted that primacy of tax Treaty over GAAR should be maintained and the arrangement entered after compliance of the conditions spelt out in treaty should be kept out of the provisions of the GAAR.

4.15.2. GAAR in light of BEPS - Overlapping of the GAAR provisions with the anti-abuse provisions introduced through the Multilateral Instrument

GAAR as they stand in their current form, leave a lot of uncertainty and doubt on their practical application due to their very wide import.

On the other hand, the overwhelming support for the Base Erosion and Profit Shifting ('BEPS') project of the Organization of Economic Cooperation and Development ('OECD') and the speed at which it has progressed is testament to the importance that globally governments are attaching to countering tax practices inspired by BEPS activities.

If we look at the two concepts together, namely the BEPS project and GAAR, their ultimate motive is the same. However, the actions set out under the BEPS project are specific and detailed, whereas the GAAR is an all-encompassing, anti-avoidance provision.

India has signed the 'Multilateral Instrument' (MLI) in accordance with the Base Erosion Profit Shifting (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 on MNE's) which are subjected to anti-abuse provisions under the tax treaty pursuant to 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 foot print in India with a clarity on the domestic tax laws prevalent in the country.

The BEPS Action Plans are poised to considerably restrict and control abusive cross border tax practices. Accordingly, it is desirable that any further action in India is co-ordinated with the BEPS actions instead of multiplying legislations. It is accordingly recommended that GAAR should not apply to a transaction/arrangement where the same is otherwise covered under the BEPS Action Plan/s.

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 Principle Purpose Test ('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.

4.15.3. 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 substantial commercial purpose 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.

Suggestion

- 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.

4.15.4. 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 **deferral of tax** 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) **a reduction in total income; or***

*(f) **an increase in loss,***

*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 INR 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[2], 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[3], 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.

[2]Page 48 and 49 of the Final Report by the Expert Committee on GAAR chaired by Dr. Parthasarathi Shome.
[3]Page 47 of the Final Report by the Expert Committee on GAARchaired by Dr. Parthasarathi Shome.

Suggestion

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'.

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.

4.15.5. Appeal against directions of Approving Panel

Section 144BA of the Act provides that the directions, issued by the Approving Panel shall be binding on the taxpayer and the Commissioner, and no appeal under the Act shall lie against such directions. In the absence of any right to appeal under the Act, the taxpayer will only have an option to file a writ to challenge the directions of the Approving Panel.

The provisions need to be amended to state that the directions issued by the Approving Panel can be appealed with the Tribunal and higher forums.

4.15.6. Other Points

- **Threshold for invocation of GAAR:** As per Rule 10U, the provisions of GAAR do not apply to an arrangement where the tax benefit arising to all the parties to the arrangement in the relevant AY (AY) does not exceed Rs. 3 crore in aggregate. This threshold limit should be further enhanced so as to capture only highly sophisticated structures.
- **Negative list:** A distinction between tax mitigation and tax avoidance should be made to ensure that legitimate business choices do not result in the invocation of GAAR. To ensure clarity, as recommended by the Shome Committee, an illustrative negative list of such instances where GAAR cannot be invoked should be issued.
- **Appointment of Approving Panel Members:** Section 144BA currently provides for the constitution of the Approving Panel by the Central Board of Direct Taxes. Mindful of the need to demonstrate independence in the applicability of GAAR, the power to make appointments to the Panel should be vested in an independent committee comprising of (a) the Chairman of the Central Board of Direct Taxes, (b) the Secretary, Ministry of Law and Justice and (c) the President of the Income-tax Appellate Tribunal.
- **General Rulings:** The Finance Act, 2012 specifically permitted a taxpayer to make an application to the Authority for Advance Rulings (AAR) for a determination as to whether a proposed arrangement is an 'impermissible avoidance arrangement'. While this is a welcome step, considering the backlog of pending matters with the AAR, it may be useful if the Approving Panel can additionally provide/ issue 'General Rulings' on several common transactions setting out in detail the various parameters that must be met, if a transaction is to avoid being characterized as an 'impermissible avoidance arrangement'. This may be done to supplement the examples given to illustrate various aspects of the GAAR.

- **Annual Summary by Approving Panel:** With a view to building up a body of guidance clarifying the applicability of the GAAR, the Guidelines should require the Approving Panel to summarise and publish a synopsis of each case dealt with by the Approving Panel (duly summarized and anonymised to preserve taxpayer confidentiality) on an annual basis. A similar recommendation has been made by the Aaronson Committee in connection the proposed GAAR in the United Kingdom[4].

- **Law Officers:** As stated above, the Commissioner should be required to independently review the legal and factual basis of invocation of the GAAR and to specifically address the issue of whether the invocation of GAAR in a particular case would stand up to judicial scrutiny. In arriving at this conclusion, the Commissioner must be required to refer the case to appropriate law officers of the Government of India (i.e. the Additional Solicitor General of the jurisdictional High Court) to ascertain his/her views as to the legal basis for invocation of GAAR.

- **Periodic Review:** In order to assess the broader impact of GAAR on the overall economic and investment climate and to evaluate its working, an expert committee comprising of independent members should be set up after 3 years to review the overall working of the GAAR in India and make recommendations as to (i) whether it should be retained (ii) whether any systemic changes in the law / departmental guidelines need to be made to ensure its smoother working.

4.16. Tax Incentives and Benefits

4.16.1. Expenditure on scientific research Sections 35(1)(ii), 35(1)(iia), 35(1)(iii), 35(2AA) and 35(2AB)

Issues

- As per the aforesaid sections, the expenditure on scientific research is allowed as weighted deduction up to 125% to 200% of the expenditure incurred. The Finance Act, 2016 has made changes in the aforesaid sections by restricting the weighted deduction to 150% if it is currently more than 150% with effect from previous year 2017-2018 and to 100% with effect from previous year 2020-21.Further, where the weighted deduction is less than 150%, it is to be reduced to 100% from previous year 2017-18.

  It is well recognised that scientific research is the lifeline of business in all countries of the world. Indian residents are paying huge sums by way of technical services, fees to foreign technicians to upgrade their products and give the customers what latest technology gives globally. If In-house research is continuously encouraged, outgo on account of fees for technical services will reduce and this will help indigenous businesses to grow. Withdrawal of weighted deduction in respect of scientific research expenditure will put a dent to the 'Make in India' initiative of the Government.

[4]p8, *A study to consider whether a general anti-avoidance rule should be introduced into the UK tax system*, Report by Graham Aaronson QC available at http://www.hm-treasury.gov.uk/tax_avoidance_gaar.htm

4.16.2. Issues related to deduction under section 35(2AB)

- 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 will put a dent to the 'Make in India' initiative of the Government.
- 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. The High Court has held that Explanation to section 35(2AB)(1) of the Act does not require that expenses included in said Explanation are essentially to be incurred inside an approved in-house research facility.

  It may be noted that the 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. 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.

  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.

- India is globally recognised 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. 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 manufacturing/research powerhouse.
- 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.
- The weighted deduction under section 35(2AB) of the Act is not available while computing book profit for the purpose of MAT provisions, which dilutes the benefit provided under section 35(2AB) of the Act as R&D in all sectors, especially biotech, pharma, etc. is very expensive and time consuming.
- 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.
- It has been observed that the 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 involve substantial expenditure does not get the benefit of 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.

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 continued to promote research and development in the manufacturing space and to make India a manufacturing hub.
- 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.
- It is recommended that weighted deduction of expenditure as per section 35(2AB) of the Act should also be allowed while computing book profit under Section 115JB of the Act.
- Explicit provisions should be introduced in the Act, to provide that DSIR can approve the R&D facilities of the companies engaged in development and sale of software. It is further recommended that weighted deduction for R&D expenditure be extended to service sector as well.
- It is recommended to provide weighted deduction for expenditure incurred on internally developed intangible assets under Section 35(2AB) of the Act. It is also recommended that any initial cost paid for acquiring R&D related intangible assets, which are used in the R&D unit should also be allowed for weighted deduction under Section 35(2AB) of the Act.
- It is recommended that 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 suggested that suitable provision should be made in section 35(2AB) of the Act to provide that once the approval is granted under section 35(2AB) the same should be effective from the date of initiation of the said research and development facility and the entire expenditure incurred on establishment of such facility should be allowed as deduction under section 35(AB) of the Act.

4.16.3. Section 35AC – Expenditure on eligible projects or schemes

Any expenditure incurred on eligible projects or schemes for promoting the social and economic welfare of the society is allowed as deduction to the extent of the amount of expenditure under section 35AC of the Act. Rule 11K of the Income-tax Rules, 1962 ('the Rules') provides the list of projects which are eligible for deduction under section 35AC of the Act. The projects as mentioned in Rule 11K of the Rules are for the development of the economically and socially weaker sections of the society e.g.; construction of school and dwelling units for economically weaker sections of society etc. After the amendment made by the Finance Act, 2016 in section 35AC of the Act, no deduction shall be available for any expenditure incurred on eligible social development project or scheme on or after April 1, 2017. Corporates contribute huge sums for this cause under their responsibility towards the society and the environment as also to fulfil conditions relating to Corporate Social responsibility ('CSR') funding. The whole initiative for the rural development and the upliftment of the poor may take a backseat, if no deduction is made available under section 35AC of the Act.

Further, the CBDT Notification NO. SO 1103(E) [NO.3/2016 (F.NO.V.27015/1/2016-SO (NAT.COM)], dated 15 March 2016 carries an exclusion that contributions received pursuant to CSR obligation shall not be eligible for deduction under section 35AC of the Act. This is contrary to the provisions of section 35AC of the Act read with Rule 11K of the Rules which do not contain any such restriction. It may be noted that Circular No. 1/2015 dated 21 January 2015 issued by CBDT explaining the amendments by Finance (No. 2) Act 2014, provides that the CSR expenditure which is of the nature described in section 30 to 36 of the Act shall be allowed as deduction under those sections subject to fulfilment of conditions, if any, specified therein. Hence, the exclusion provided in the aforesaid notification conflicts with the provisions of section 35AC of the Act and the Circular No. 1/2015 (supra).

The expenditure incurred on eligible projects or schemes are for the development of the backward and weaker sections of the society. Further, all the projects are approved by the National Committee which is set up by the Central Government to ensure that the funds are utilized for the said purpose. Therefore, this deduction which is serving a useful purpose for which it was enacted, should be continued to be allowed at least for three more years. Further, the disqualification for CSR contributions in the aforesaid notification approving section 35AC projects should be immediately withdrawn and it should be clarified that CSR contributions to section 35AC approved projects are allowable as deduction under section 35AC of the Act.

4.16.4. Allow weighted deduction of capital expenditure under section 35AD of the Act

Section 35AD(1A) provided weighted deduction in respect of the capital expenditure (other than land/ goodwill/ financial instrument) to a taxpayer engaged in following business:

- Setting up and operation of cold chain facility;
- Setting up and operation of warehousing facility for storage of agricultural produce;
- Building and operating a hospital with more than 100 beds;

- Building housing project under a scheme for affordable housing framed by the central government or state government and notified by Central Board of Direct Taxes;
- Production of fertilisers.

However, with effect from AY 2018-19, deduction under section 35AD of the Act is restricted to 100% of the expenditure only. It is recommended that the weighted deduction available to a taxpayer engaged in specified business be restored for another 5 years. It is further believed that there is a need to promote the infrastructure sector in India. Accordingly, the benefit of weighted deduction must also be provided to new infrastructure facility covered under section 35AD(8)(c)(xiv) of the Act.

Deduction under Section 35AD of the Act is an alternate form of accelerated deduction for the capital expenditure in the specified business. However, the cash flows of these capital intensive industries suffer on account of levy of MAT. This is because book profit continue to be higher than taxable profits (given that deduction for capital expenditure is not taken to the profit and loss account other than in the form of depreciation) and hence, MAT is paid by the industry during the incentive period. Further, given the restriction on the years for carry forward of MAT, it is possible that MAT paid in initial years may not be recovered, especially for those taxpayers who have a longer period before reaching break-even.

It is suggested that the Government should consider reducing the rate of MAT more so for the infrastructure sector as levy of the same defeats the very purpose of extending tax incentives to the industry, especially given the high rate of MAT now.

4.16.5. 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. 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.

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

Issues

- The amendment to Section 35AD(3) of the Act carried by the Finance Act, 2010, seeks to prevent 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 non-satisfaction 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.

4.16.7. Section 35CCD – Expenditure on skill development project

Section 35CCD provides for weighted deduction of expenditure incurred on skill development project. This project should be approved from National Skill Development Agency (NSDA) and should be carried out in a separate training institute. This training institute should also be separately affiliated with either National Council for Vocational Training (NCVT)/ State Council for Vocational Training (SCVT) or empanelled with NSDA.

Issues

Currently, no guidelines are available to get these training institutes affiliated with NCVT/ SCVT or empanelled with NSDA. Draft guidelines dated 30 April, 2014 in this respect were forwarded by NSDA to various ministries for their comments, however there is no visibility on its progress.

Further, affiliating training institutes with NCVT/SCVT or NSDA is an onerous and a time consuming process which is difficult and to some extent impractical for corporates.

Further, the Finance Act 2016 has restricted the claim of deduction from 150% of the expenditure to 100% of the expenditure from AY 2021-22. Given that, the approvals are time consuming and skill development is one of the motives of the government, it is also suggested that the sun-set for restricting the deduction to 150% to 100% may be removed.

Recommendations

- The guidelines for getting the training institutes affiliated with NCVT/SCVT or empanelled with NSDA should be finalised at the earliest.
- Extend benefit of Section 35CCD to shop-floor trainings also, besides separate training institutes. The shop-floor training may be when empanelled and approved by NSDA.
- Extend the earlier benefit of deduction of 150% of the expenditure.
- Expenditure incurred on training to new workforce or expansion of workforce to meet business needs (e.g. in service industry which deploys new workforce for business expansion) should also be made eligible for deduction under this section.

4.17. Carry Back of Losses - Section 72

Issue and Recommendation

- It is has been observed that provisions relating to carry-back of business losses are prevalent in many developed countries like United States of America, Singapore, United Kingdom etc. In case of carry back of losses, losses are allowed to be offset with the profits of the previous years.

  Such provisions should also be introduced in the Act and carry back of losses up to 3 to up to 3 to 5 years should be allowed.

4.18. Deduction under Section 80JJAA of the Act

Issues

- The Finance Act, 2016 has liberalised the conditions for allowability of deduction in respect of employment of new employees by amendments in section 80JJJAA of the Act. However, one of the conditions stipulated by the section is that an employee should be employed for a period of two hundred and forty days or more during the previous year of employment. In a situation, where an employee worked for less than 240 days in the relevant previous year of employment i.e. in Year 1 but for full year in Year 2 and Year 3 and assuming all other conditions prescribed in Section 80JJAA of the Act are complied with, the assesse is still not eligible to claim deduction in any of the years.
- It is not clear as to whether the deduction is in the nature of standard deduction whereby the quantum is ascertained with reference to additional wages paid in Year 1 and 30% thereon is allowed in Years 1 to 3 or is it linked to wages paid to qualifying workers in each of the years 1 to 3. There could be variation in the amount of deduction in Year 1, 2 and 3 based on wages paid to the same worker.
- The limit of total emoluments of Rs. 25000 per employee per month to be eligible for benefit under this section is very less and be increased to at least Rs. 50000 per month.

Recommendations

- It is recommended that amendment be made in section 80JJAA of the Act to provide that employees in respect of whom the period of continuous employment of 240 days or more is attained in the previous year succeeding the previous year in which he is employed, the deduction under section 80JJAA of the Act should be granted from the succeeding previous year.
- It may also be clarified that the deduction under section 80JJAA of the Act is in the nature of standard deduction for Years 1 to 3 based on additional wages paid in Year 1.
- The limit of total emoluments per employee of Rs. 25000 per month be increased to at least Rs. 50000 per month

4.19. Issues – Circulars and Notifications

4.19.1. Applicability of CBDT Circular on Formation of AOP vis-à-vis the EPC Contracts

The term Association of Persons (AOP) has not been defined in the Act. As per Section 2(31) of the Act, 'person' includes association of persons or body of individuals, whether incorporated or not. Explanation to Section 2(31) of the Act further provides that an AOP shall be deemed to be a person, whether or not such person or body was formed or established or incorporated with the object of deriving income, profits or gains. Consortium of contractors is often formed to implement large infrastructure projects, mainly in Engineering, Procurement and Construction (EPC) contracts and turnkey projects. The tax authorities have often taken a view that such consortium constitutes an Association of Persons ('AOP') for charging tax and which has led to a significant tax disputes.

4.19.2. CBDT Circular No. 7 of 2016, dated 7 March 2016

With a view to avoid tax disputes and to have consistency in approach, CBDT vide Circular No. 7 of 2016, dated 7 March 2016 has laid down certain attributes which would not lead to constitution of an AOP:

- Each member is independently responsible for executing its part of work through its own resources and also bears the risk of its scope of work i.e. there is a clear demarcation in the work and costs between the consortium members and each member incurs expenditure only in its specified area of work.
- Each member earns profit or incurs losses, based on performance of the contract falling strictly within its scope of work. However, consortium members may share contract price at gross level only to facilitate convenience in billing.
- The men and materials used for any area of work are under the risk and control of respective consortium members;
- The control and management of the consortium is not unified and common management is only for the inter-se co-ordination between the consortium members for administrative convenience.

The above stated Circular has provided clarity to a certain extent. However, some of the issues emanating from the circular are as below:-

Issue

- The Circular states that it shall not apply where all or some of the members of the consortium are Associated Enterprises (AE) under Section 92A of the Act. In such cases the AO shall decide whether an AOP is formed or not, keeping in view the relevant provisions of the Act and judicial precedents on the issue. There does not appear to be any reason to exclude related parties from the purview of the above circular to determine the existence of AOP or not. In fact, similar principles should also be applicable to determine the existence or otherwise of an AOP in situations where some of the parties to the consortium are related to each other.

Recommendation

- It is suggested that the benefit of the aforesaid circular should also be extended to AE situations where such AEs are members of the consortium for executing EPC/turnkey contracts. It is recommended that definitive guidelines must be provided even in case of associated enterprises with adequate checks.

4.19.3. Notification No 53 dated 24 June 2016 (Relaxation in requirement to furnish PAN)

The CBDT vide Notification 53/2016 has notified new Rule 37BC which states that provisions of section 206AA (requiring deduction of tax at a higher rate) shall not apply on payments in the nature of interest, royalty, fees for technical services and payments on transfer of any capital asset provided the non-resident (deductee) furnishes following prescribed documents:-

- Address in the country or specified territory outside India of which the deductee is a resident;
- Name, e-mail id, contact number;
- A certificate of his being resident in any country or specified territory outside India from the Government of that country or specified territory if the law of that country or specified territory provides for issuance of such certificate;
- Tax Identification Number of the deductee in the country or specified territory of his residence and in case no such number is available, then a unique number on the basis of which the deductee is identified by the Government of that country or the specified territory of which he claims to be a resident.

While the above is a very welcome Notification which will obviate hardships caused by several non-residents who suffer withholding at a higher tax rate, the following should also be clarified:-

- Relaxation in requirement to furnish PAN should be made applicable on all types of payments and should not be restricted only to interest, royalty and fees for technical services.

- Also, in order to remove any potential ambiguity, it should be expressly clarified that treaty benefits will continue to be available even in absence of PAN provided the requisite documents as prescribed are furnished.
- Further, in order to avoid such protracted litigation, the relaxation granted vide this notification should also apply to pending assessments and appeals provided the requisite documents as mentioned in the Notification are furnished.

4.19.4. Office Memorandum dated July 31, 2017 (Guidelines for Stay of Demand)

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 Income-tax (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 lumpsum 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 pre-deposit 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.

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 favorable 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[5]. 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).

4.19.5. 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

[5] HDFC Bank Ltd (354 ITR 77), Mauri Suzuki India Ltd (347 ITR 43)

business income in case where shares of unlisted companies are held as stock in trade on a consistent basis.

4.19.6. Circular No. 4/2016 dated 29 February 2016

- In this Circular, the CBDT has clarified that where a consideration is payable towards a contract for production of content for a broadcaster/ telecaster (where rights in such content are also transferred to the broadcaster/ telecaster); such a contract is covered by the definition of 'work' as per section 194C of the Income Tax Act, 1961.

  However, it should additionally be clarified that in a case where 'funding' is provided by the broadcaster to the production house for production of content, no TDS obligation should arise on the broadcaster provided the amount of 'funding' represents a pure "reimbursement" of cost (without any mark-up) on which appropriate tax withholding is already done by the production house.

4.20. Non-Resident related provisions

4.20.1. 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 non-resident 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 non-resident 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 NR 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.

4.20.2. Provisions 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.

  The non-exclusion of listed company shares from the ambit of the indirect transfer provisions will cause serious hardship to shareholders in several listed companies as well as pose several computational and practical challenges in cases where frequent trading of shares takes place on a daily basis.

  Such cases also pose significant challenges from the point of view of withholding, given that the very identify of the seller is not ascertainable. Further challenges exist in respect of ascertaining whether the seller holds more than 5% or not, whether he qualifies for treaty benefits, his cost of acquisition etc.

  Even if one were to take the view that withholding is merely a tentative determination of tax, and is subject to the correct determination at the time of assessment, the practical challenges in requiring millions of investors in stock markets around the world to obtain a TAN in India, deduct tax, and deposit the same with the government, and issue TDS certificates without even knowing the identity of the person on whose behalf such tax is deposited are simply mind-boggling. Further, there would be no basis on

which such buyers could even issue TDS certificates since the identity of the seller would not be known.

In view of the above, 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.

- Explanation 5 to Section 9(1)(i) of the Act provides that an asset or a capital asset being any share or interest in a company……".It is not clear as to whether all and any type of asset will be covered by this Explanation or it will be restricted to only capital asset in the nature of share or interest in an entity. Therefore, clarity is required on interpretation of this phrase.

- In the context of amalgamations and demergers, section Act 47 of the Act provides for exclusion from capital gains tax subject to certain conditions. However, these exclusions are proving inadequate, with increased cross border economic activity and transactions.

  For instance, although specific exemptions are provided for under section 47 for companies which are amalgamated/demerged in an offshore transaction that gives rise to indirect transfer tax in India, no corresponding exemption has been provided to the shareholders of such companies. This may be contrasted with the position in respect of domestic amalgamations/demergers where exclusion is provided in section 47 at both the company and the shareholder level.

  Similarly, no exemption is provided for Indian shareholders owning shares in foreign companies which undergo an amalgamation/demerger.

  Given the above, it is recommended that a specific provision along the lines of section 47(vii) of the Act may be inserted to protect shareholders of foreign amalgamating/demerged company. These must be provided for in the Act at the earliest.

- 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) 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) 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 indirect transfer related provisions does not apply to any investment held by a non-resident, directly or indirectly, in a FII registered as category I or category II FPI under the SEBI (FPIs) regulations, 2014, with effect from 1 April 2012. It is suggested that this exemptions should also be extended to category III FPI.
- As per section 285A of the Act, the Indian entity is required to furnish information relating to indirect transfers. In case of any failure, the Indian company will be liable for a penalty of INR 500,000 or 2% of the value of the transaction as specified.

  Considering the exhaustive list of information and documentation along with penal consequences for default (as envisaged in section 271GA), it is extremely onerous obligation on the Indian concern and it is farfetched that the Indian concern will be able to collate all such information.

  There are a large number of Indian companies that have raised capital from funds that invest in Indian companies through layers of investment holding entities. On grounds of confidentiality, the information on the investment holding entities and group entities is unlikely to be placed at the disposal of the Indian concern.
- It is recommended that the flexibility to comply with the reporting obligation under Rule 114DB be provided i.e. the reporting obligation should be complied either by the Indian concern or the transferor or transferee where the transfer of share/interest in the foreign company/entity is covered by provisions of section 9(1)(i) of the Act. As next best alternative, reporting obligation must be limited to a case where the transaction results in change in control and management of Indian company.

  Also, 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.

  Provide a simple reporting obligation which shall comprise of base information such as details of transferor, transferee, subject matter of transfer and its valuation (similar to practice followed by Peru and Chile).
- The obligation of Indian concern should be restricted to the extent such Indian concern is possessed of information and/or documents. There should be no penal consequences in the event of failure to report, except when there is a misrepresentation.
- The Indian concern may be obligated to furnish information only in a case where the transfer is liable to tax under section 9(1)(i) of the Act. It may be explicitly provided that if the transferor is entitled to small shareholders exemption or avails treaty exemption or if transfer is exempt in terms of section 47 of the Act; there may be no corresponding

obligation on the Indian concern as the transfer would not attract to tax under section 9(1)(i) of the Act.

- The expression *"Indian concern"* may have different meanings. It may even encompass permanent establishment or other forms of permanent establishments of a foreign company. Clarity needs to be provided on this aspect also.

4.20.3. 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.

4.20.4. 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.

4.20.5. Clarity on Issue of Deduction of Tax at Source on Export Commission Paid to Non-Resident Agents

The CBDT had issued Circular no. 23 dated 23 July 1969, clarifying that commission paid to non-resident agents during the course of export was not taxable in India. Further, vide circular no. 786 dated 7 February 2000, the CBDT had again stated that, such commission paid to non-resident agents was not taxable in India under section 5(2) and 9 of the Income Tax Act, 1961 ('the Act') and no tax is therefore deductible under section 195 of the Act.

CBDT vide Circular No. 7/2009 dated 22 October, 2009 withdrew the circulars No 23 dated 23rd July, 1969, No. 163 dated 29th May, 1975 and No. 786 dated 7th February, 2000. The reason stated by CBDT in its 2009 circular was that the circular cannot be interpreted to allow relief to the taxpayer which is not in accordance with the provisions of section 9 of the Income-tax Act or with the intention behind the issue of the Circular. The 2009 circular also stated that it has been noticed that interpretation of the Circular by some of the taxpayers to claim relief is not in accordance with the provisions of section 9 of the Income-tax Act, 1961 or the intention behind the issuance of the Circular.

From perusal of the circular no.7/2009, it is understood that the intention of the Government behind withdrawal of circular no. 23/1969 is not to override the provisions of section 5 and section 9 of the Act. However, the withdrawal of aforesaid Circulars does not necessarily mean that a non-resident would now be liable to tax in India in the situations described in Circular No 23. The taxability of a non-resident taxpayer, under the Act, would need to be evaluated, independent of the position stated in the above Circulars, having regard to the provisions of the Act and relevant judicial precedents. In general, the tax position described in Circular No 23 can be viewed as merely clarifying the position of law and in a number of instances, Courts have reached a similar conclusion independent of Circular No 23. Thus, even if the aforesaid Circulars have been withdrawn, the legal position with respect to the taxability of the commission paid to foreign agents has not changed in view of section 9 of the Act and judicial pronouncements are in favour of the taxpayers. The Hon'ble Supreme Court in the case of CIT v. Toshoku Limited (1980) (125 ITR 525)(SC) has held that considering the statutory provisions of the Act, the commission amounts which were earned by the non-resident for services rendered outside India cannot be deemed to be income which has either accrued or arisen in India. It was also held that the non-resident agent did not carry on any business operations in the taxable territories as contemplated by Explanation 1(a) to Section 9(1)(i) of the Act. The position has been reaffirmed by the various courts that even after the withdrawal of circular no. 23 (supra), the commission paid to non-resident is not liable to tax under the Act when the services were rendered outside

India, services were used outside India, payments were made outside India and there was no business connection of the non-resident in India.

Even assuming that the non-resident agent has a business connection in India, as no operations, per se, are carried out by him in India, as per Explanation 1(a) to section 9(1)(i) of the Act, no income can be attributed in India and hence taxed in India. This principle has been affirmed by the Hon'ble Supreme Court in the case of Carborandum vs CIT (108 ITR 335) as well as in the case of Toshoku Ltd (supra).

However, by withdrawal of circular no. 23 (supra), the commission paid to non-resident agents for the purpose of export is being perceived by the tax authorities as taxable in India in virtually all the cases. The tax officers are not giving cognizance to the facts of the cases and judicial precedence relied upon by the taxpayers. Consequently, a large number of Indian companies are facing the issue of disallowance of the expense in respect of the said commission and have been served notices with huge demands for failure to deduct tax at source on the commission paid to its foreign agents.

The arbitrary disallowance of the export commission by the tax officers in the hands of the Indian company has created widespread litigation. This is gravely affecting the cash flow of the companies and is acting as a hindrance for the Indian companies to develop their market internationally.

Recommendation

It is requested that the Government may clarify that the commission payment to non-resident agents is not taxable in India if they do not fall within the purview of section 5 and section 9 of the Act. It should be further clarified that the tax withholding obligation in the hands of the payer would not arise if the commission is not chargeable to tax under the Act, irrespective of whether a specified declaration from the revenue authorities, under section 195 of the Act, has been obtained or not.

4.20.6. Review of Retrospective Amendments made by Finance Act, 2012

(a) Clarification on Definition of Software Royalty – Section 9(1)(vi)

In Section 9(1)(vi) of the Act, Explanation 4 has been inserted with effect from the 1 June 1976, clarifying that the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a computer software (including granting of a licence) irrespective of the medium through which such right is transferred.

Royalty internationally applies to payments for use of a copyright, patent, trademark or such intellectual property. As per international commentaries and jurisprudence, any payments for use of a copyrighted article would not typically get covered under the term 'Royalty'. The Government should consider the adversity of the amendments made by Finance Act, 2012 on the businesses and make changes in the law to reverse its effect. It is suggested to roll back Explanation 4 to Section 9(1)(vi) of the Act. Further, it is suggested that in view of the international tax practices and keeping in mind the impact on Indian industry, it should be clarified that the payments for use of copyrighted software made to non-residents would

not be covered under the definition of 'royalty'.

Alternatively, the amendment should have only prospective application.

(b) Clarification on Inclusion of Explanation 5 to Section 9(1)(vi) of the Act

In Section 9(1)(vi) of the Act, Explanation 5 has been inserted clarifying that royalty includes and has always included consideration in respect of any right, property or information, whether or not:-

(a) the possession or control of such right, property or information is with the payer;

(b) such right, property or information is used directly by the payer;

(c) the location of such right, property or information is in India.

Issues

- Explanation 5 conflicts with the existing Explanation 2 to Section 9(1)(vi) of the Act in as much as there cannot be any transfer, right to use or imparting without the possession or control in the right, property or information vesting with the buyer/ payer. Explanation 5 also has the effect of taxing the consideration as royalty even if there is no transfer, right to use or imparting of any right, property or information to the payer.
- The provisions of this explanation are also not in line with the internationally accepted principles.
- By virtue of the above amendment, the scope of the term Royalty gets expanded to cover payments which are not intended to be covered. The mere fact that a transaction involves use of equipment by a service provider, without the customer having control/ physical possession of such equipment, payment for such facility/ services cannot be treated as royalty. For example, where a person boards a bus or train by purchasing the requisite ticket, it cannot be said that the person is making payment for availing the bus or train on hire as he does not have the control over such equipment. Rather the customer is merely availing the facility of transportation, the consideration for which facility is not in the nature of Royalty.
- It appears that the above provisions may also cover payment for a number of e-commerce transactions like access to databases, etc. which is not royalty in true sense. Even internationally, a large variety of e-commerce transactions are not covered within the ambit of “royalty”. Some examples of such payments are:-
    - Transactions relating to access to online subscription database;
    - Payment by portal companies to ISPs for website hosting;
    - Payments for downloading content online;
    - Payment towards securing space from cloud for order completion, inventory information etc. without the Indian Payee acquiring rights/control over space, etc.
    - Goods on digital medial (e.g. e-books, music videos, etc.). These goods otherwise would not have amounted to “royalty”. Say, where a book is purchased from a book

shop may not amount to royalty, however, when purchased from an online website could amount to “royalty”.

- Distribution rights are also at times treated as “royalties” e.g. movies/ programmes distributed through Apps or e-commerce website.

- It has been held by various Courts that the information that is available in public domain is collated and presented in a proper form by applying the taxpayer's methodology and the payment for the same is not to be construed as royalty. It is in line with the international standards and supported by the OECD commentary, which provides that data retrieval or delivery of exclusive or other high value data cannot be characterized as royalty or FTS.

- Hence, given the above, it may be provided that transactions of the above nature be excluded from the definition of “royalty”.

Recommendations

- It is suggested that Explanation 5 to Section 9(1)(vi) of the Act inserted by the Finance Act, 2012 may be omitted altogether, as this is clearly against the basic principle of the definition of the term royalty provided under Explanation 2 clause (iva) and as also understood internationally. It is recommended to suitably exclude the payment for the use/access to online databases, reports, journals etc. and any other such payments made by the payer from the purview of royalty.

- Alternatively, in order to avoid ambiguity, the amendment should be modified to objectively provide the rationale behind the insertion of the Explanation 5 and should also clarify that the transactions of the nature mentioned above are excluded from the definition of “royalty”.

- Alternatively, the amendment should have only prospective application.

(c) Clarification on Definition of Process Royalty – Section 9(1)(vi)

In Section 9(1)(vi) of the Act, Explanation 6 was inserted, with retrospective effect from the 1st June 1976, clarifying that the expression 'process' includes and shall be deemed to have always included transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fibre or by any other similar technology, whether or not such process is secret.

Issues

- The amendment may result in inclusion of charges for the use of transponder capacity or connectivity/ bandwidth within the definition of 'Royalty'.

- Services in the nature of provision of transponder capacity or connectivity/ bandwidth are merely facilities provided. As per international tax practices and OECD Commentary, payments for such facilities should not be treated as 'royalty'.

- Explanation 6 even includes payments towards provision of basic telephone service within the ambit of the term ‘royalty’. The business income derived by the telecom

providers, if classified as royalty, will significantly alter the tax consequences on the receiver of the consideration for the services provided and will burden the payer with TDS compliances.

- Taxation of foreign companies for such facilities and subsequent passing on of the tax cost to India Inc. entail a significant tax outgo for India Inc., especially companies operating in the field of media and entertainment (satellite and broadcasting companies), IT and ITES companies and telecom.
- The retrospective application of the amendment is grossly unfair and further aggravates the situation.

Recommendations

- In line with international practices and the OECD Commentary, it is suggested that the terms 'transmission', 'up-linking', 'amplification', 'downlinking' could be specifically defined in the Act to remove ambiguity on its scope/coverage in the definition of 'royalty'.
- The definition of the term 'transmission' should explicitly clarify that payments for the use of a 'facility' as a service charge, without any control on the process and where the payer is only interested in the service and not in the use of process, should not be covered within its meaning.
- A clarification should be provided that basic services such as telephone/mobile charges and broadband/ internet connectivity charges, payment to cable operators for viewing the television channels, electricity charges, wheeling/transmission charges paid to state electricity grid or to private electricity transmission companies would be outside the ambit of royalty.
- Alternatively, the amendment should have only prospective application.

4.20.7. Requirement for Non-residents to comply with TDS Obligations - Section 195

The Finance Act, 2012 extended the obligation to deduct tax at source to non-residents irrespective of whether the non-resident has:-

(i) a residence or place of business or business connection in India; or

(ii) any other presence in any manner whatsoever in India.

The aforesaid amendment was introduced with retrospective effect from 1 April 1962.

Issue

The amendment results in a significant expansion in the scope of TDS provisions under the Act and will cover all non-residents, regardless of their presence/connection with India.

The Supreme Court in the case of Vodafone International Holdings B.V. [(2012) 345 ITR 1 (SC)] has observed that tax presence is a relevant factor in order to determine whether a non-resident has an obligation to deduct tax at source under Section 195 of the Act. The amendment by the Finance Act, 2012, however, seeks to expressly extend the scope of tax deducted at source (TDS) obligations to all persons including non-residents,

irrespective of whether they have a residence/ place of business/business connection or any other presence in India.

Recommendation

- The amendment (inserted by way of an Explanation) should be removed as it causes undue hardship to persons who genuinely do not have any income chargeable to tax in India.
- The amendment should be modified to restrict the applicability of TDS provisions to residents and non-residents having a tax presence in India.

4.20.8. Cascading effect of DDT on dividend received from Foreign Companies-Section 115-O

As per the amendment in Section 115-O of the Act vide Finance Act 2013, dividend taxed as per Section 115BBD of the Act received by the Indian company from its foreign subsidiary (i.e. where equity shareholding of the Indian company is more than 50%), then any dividend distribution by such Indian Holding Company to its shareholders in the same FY to the extent of such foreign dividends will not be liable to DDT.

Issue

- As per Section 115BBD of the Act, dividend received from a specified foreign company i.e. a foreign company in which the holding of the Indian company is 26% or more in the nominal value of equity share capital, is subject to tax at a lower rate of 15%. However, as per provisions of Section 115-O of the Act, where dividend is received from a foreign subsidiary (i.e. more than 50% equity shareholding) which is subject to tax @15% under Section 115BBD of the Act, then such dividend will be reduced from the DDT base on any further dividend distributed by the Indian company. In other words, where the Indian company holds 26% to 50% in nominal value of the equity share capital of the foreign company, then such dividend would not be excluded for computing DDT base of the Indian parent.
- Additionally, the benefit of reduced rate of tax on dividends as per Section 115BBD of the Act is restrictive and is available only to Indian companies only and not to other persons.

Recommendation

- It is suggested that the requirement relating to shareholding of more than 50% in the foreign subsidiary for the purpose of Section 115-O of the Act should be reduced to 26%, to remove the cascading effect of DDT. Also, the objective of incentivizing repatriation of funds shall be successful when the dividend received from a specified foreign company and distributed by the Indian company is not liable to DDT, thereby removing the cascading effect.
- The reduced rate of tax on dividends received from a specified foreign company should also be extended to all persons (including a company) as defined in Section 2(31) of the Act.

4.20.9. Applicability of Rule 37BB read with Section 195

Issues

- Amended Rule 37BB(3)(i) of the Rules exempts remittances as per the provisions of Section 5 of the FEMA read with Schedule-III i.e. only current account transactions.

As per Section 5 of the FEMA, any person may sell or draw foreign exchange to or from an authorised person if such sale or drawl is a current account transaction provided that the Central Government may, in public interest and in consultation with the Reserve Bank of India, impose such reasonable restrictions for current account transactions as may be prescribed.

The Master Direction No. 7/2015-16 dealing with the Liberalised Remittance Scheme (LRS) is a liberalisation measure to facilitate resident individuals to remit funds abroad for permitted current or capital account transactions or combination of both.

The press release issued by the CBDT on 17 December 2015 states that Form 15CA and 15CB will not be required to be furnished by an individual for remittances which do not require RBI approval under the LRS. However, it may be noted that LRS does not find any specific mention in the amended Rules.

LRS is a wider term as it includes within its scope both permissible capital and current account transactions. The amended Rules are silent with respect to the capital account transactions under LRS.

Recommendation

- It is suggested that capital account transactions should be specifically included in the exclusion list of Rule 37BB(3)(i) of the Rules read with Section 195(6) of the Act.

4.20.10. Penalty for Failure to furnish Information/Inaccurate information under Section 195

The Finance Act, 2015 has introduced penalty (Section 271-I of the Act) in case of failure to furnish information or furnishing of inaccurate information as required to be furnished under Section 195(6) of the Act, to the extent of INR one lakh.

Recommendation

It is not clear whether the penalty is qua the payment made or qua the transaction or qua the contractual obligations for a specific financial year. Therefore, the same should be clarified in a suitable manner.

4.20.11. TDS from Payments to Non-residents having Indian Branch/Fixed Place PE

Issue

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

compared with its Indian counterparts. This additionally requires the non-resident company to mandatorily approach the tax office to seek a lower TDS certificate, the process being time-consuming and non-taxpayer friendly. Often, the non-resident company faces a lot of difficulties justifying its request for a lower TDS certificate in the initial years of its operations, when it has no past assessments in India. From the tax officer's perspective, this results in excess tax collection by way of TDS only to be refunded later together with interest in addition to significant administrative burden, which may not be commensurate with the benefits of an efficient tax collection mechanism.

Recommendation

- It is recommended that payments which are in the nature of business income of non-residents having an India branch office or 'a place of business within India' should be subject to similar TDS requirements as in case of payments to domestic companies. Further, at the beginning of a tax year, the non-resident taxpayer who has an India branch office or 'a place of business within India' should be permitted to admit PE and opt for a TDS mechanism as is applicable to a resident company. It would go a long way in facilitating ease of doing business in India and the tax officer would be in a position to better monitor and regulate such non-resident companies. Further, it would also achieve the stated objective in the Kelkar Report (December 2002) to abolish the system of approaching the tax officer for obtaining certificates for deduction at lower rates and minimize the interface between the taxpayer and tax officer.

4.20.12. Assessee in default under section 201

Issues

- Various Indian companies make payments to foreign companies for services rendered (FTS/Installation/Consultancy etc.). This arrangement is inevitable for capital intensive technology driven companies due to inadequate vendors in India. The payments in such contracts are made based on NO PE certificate and tax residency certificate obtained from the foreign company. It may be noted that the final tax position (i.e. having a PE or not) of a foreign company in India depends on fact of the case and such facts would not be available with the Indian company. However, if later during the assessment proceedings of foreign company in India, the tax authorities hold that foreign company has a PE in India, the Indian company is held as assesse in default under section 201 of the Act for non-withholding of tax on payments to such a foreign company. It is emphasised that even though the Indian company exercised due diligence while determining TDS liability on the payment to a foreign company it is still liable to face consequences for default in non-withholding of tax.

Recommendation

- It is suggested that appropriate provisions should be introduced in the Act to provide that where the resident company exercised due diligence while making the payment to non-resident by collecting No PE declaration, TRC and Form 10F from the foreign company, no proceedings under section 201 of the Act should be initiated against the

Indian company for said payments. The requirement of obtaining a No PE certificate may be incorporated in the provisions of the law.

4.20.13. Ease tax compliance of filing tax return and transfer pricing compliance for non-residents

Issue

Section 115A of the Act provides gross based taxation in case of income earned by way of interest, dividends, royalty and fee for technical services for non-resident assessee not having permanent establishment in India. As per section 195 of the Act, in case of a non-resident, the entire tax liability of such assessee will be deducted at source by the payer on accrual/ payment and, there would be no additional tax payable by such assessee in India on such income. Despite the fact that the entire tax liability of non-resident on income referred under section 115A of the Act will be deducted at source by the payer, such assessee are still required to obtain a Permanent Account Number (PAN) and file a return of income in India.

The Finance Act 2016, in order to reduce compliance burden, amended section 206AA of the Act so as to provide that the provisions of said section shall not apply to a non-resident, not being a company, or to a foreign company, in respect of any payment, other than interest on bonds, provided non-resident provides the alternative information as prescribed.

In view of the above, in order to encourage investment in India and reduce compliance on non-residents, it is recommended that where a foreign investor's only source of income in India is from income taxable under section 115A, and, the entire tax liability of such investors is deducted at source and paid by the payer, then, the requirement for following compliance should be eliminated:

- Filing of return of income
- Filing of transfer pricing audit report where the assessee has undertaken transfer pricing compliance in home country and such transaction is at arm's length.

Recommendation

It is suggested that the provisions of section 115A(5) of the Act (non-filing of income tax return) should be extended to income earned in the nature of Royalty/ FTS wherein tax has been withheld as per the rates prescribed in section 115A of the Act.

4.20.14. Clarification regarding 'Indian Concern' under section 115A

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.

4.21. Mergers & Acquisitions

4.21.1. MAT Credit - Section 115JAA

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.
- The Finance Act, 2017 amended section 115JAA of the Income-tax Act, 1961 to provide that the tax credit in respect of Minimum Alternate Tax (MAT) paid by companies under section 115JB of the Act can be carried forward up to fifteenth assessment year immediately succeeding the assessment year in which such tax credit becomes allowable. This amendment is to be effective from 1 April, 2018. An issue arises in cases where the ten-year period has expired with the assessment year 2016-17 owing to completion of ten year period on the basis of the applicable provisions. In such cases, having regard to the amendment made, a question arises as to whether the benefit which has already lapsed will get a new lease of life. The ambiguity arises since the amended extension of carry forward period to fifteen years shall take effect only from April 1, 2018 (i.e. A.Y. 2018-19). The issue in hand needs to be addressed so that taxpayers' whose MAT credit carry forward period has lapsed should not be at a disadvantage and suffer from the transitional impact of the amendment. Accordingly, it is suggested that appropriate clarification be provided in this regard.

4.21.2. TDS and Advance Tax Credit

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.

4.21.3. 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. 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 2 years prior to transfer and by the amalgamated company for 5 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 5 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.

4.21.4. 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 49 percent or more 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.

4.21.5. Taxation of Long Term Capital Gains on Transfer of Unlisted Securities

The Finance Act, 2012 had amended Section 112(1)(c) of the Act to provide a concessional long term capital gain tax of 10% on transfer of capital assets being unlisted securities in the hands of non-residents (including foreign companies). A clarificatory amendment was further made in section 112(1)(c) of the Act by the Finance Act, 2016 to provide that long term capital gains arising from the transfer of a capital asset being shares of a company not being a company in which the public are substantially interested, shall be chargeable to the tax at the rate of 10%.

Issues

- The reduced rate of 10% under section 112(1)(c) of the Act is not available to a resident shareholder.
- The amendment made by the Finance Act, 2016 restricts the applicability of the section to 'shares' of company not being a company in which public are substantially interested as against other securities.

Recommendations

- It is suggested that the benefit of 10% rate be extended to resident shareholders also on sale of shares of a company not being a company in which public are substantially interested.
- It is further recommended that the word 'shares' following the phrase 'company not being a company in which public are substantially interested, should be replaced by 'shares and securities'.
- It should be further clarified that the section will also be applicable in case of shares and securities of a private company which is deemed to be a public company.

4.21.6. Status of Widely held Company to be considered on date of Transaction

Issues

- Section 2(18) of the Act defines widely held company. This definition has wide implication on carry forward of loss, taxability under Section 56(2) of the Act and in various other provisions.
- It includes a listed company, only if its shares are listed on exchange as on last date of the relevant year. Further, it includes subsidiary of listed company, only if the shares of such subsidiary were held throughout the relevant year by the listed company. These provisions lead to situations which does not seem intended.
- Therefore, it stands logical that the conditions of listing, holding of shares etc. should be subject matter of test on the date of transaction and should not be stretched to be continuing till the end of that FY.

Recommendation

- Section 2(18) of the Act should be suitably amended to provide test of conditions on the date of relevant transaction.

4.21.7. Deeming Fair Market Value as Full Value of Consideration for Transfer of Unquoted Shares

The Finance Act, 2017 has expanded the scope of section 56 by inserting a new clause (x) in sub-section (2) of section 56, so as to provide that receipt of sum of money or any property by any person, without consideration or for inadequate consideration in excess of Rs. 50,000 shall be chargeable to tax in the hands of recipient under the head "Income from other sources". The Finance Act, 2017 has further inserted section 50CA in the Act to provide that the sale consideration for transfer of shares other than the quoted shares shall

be deemed to be the fair market value; determined in accordance with the prescribed method, if the actual consideration is lower than such FMV.

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 the newly introduced 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.

4.21.8. 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.
- Proviso to section 56(2)(x) of the Act excludes certain receipts by relatives, certain trusts or institutions and receipt by way of certain transfers not regarded as transfer under section 47 in relation to distribution of capital assets on partition of HUF, transfer of capital asset in scheme of amalgamation, transfer in a scheme of amalgamation of banking company with banking institution, transfer of capital asset in demerger, transfer of capital asset in business reorganisation by a co-operative bank to successor co-operative bank etc.

While the amendment has exempted certain transfers arising out of amalgamation, demerger etc. there are exempt transfers under section 47, which are not forming part of the exemptions under section 56(2)(x) of the Act. As per the provisions of section 47(iv) of the Act, any transfer of capital asset by a company to its subsidiary company is exempt from tax where

- the parent company or its nominees holds the whole of the share capital of the subsidiary company; and
- the subsidiary company is an Indian Company.

Similarly as per provisions of section 47(v) of the Act, any transfer of capital asset by subsidiary company to its holding company is exempt from tax where:

- the whole of the share capital of the subsidiary company is held by the holding company; and
- the holding company is an Indian Company.

Like amalgamation/demerger such transfers between holding company and subsidiary company are undertaken with an intention of internal re-structuring. However, while exemption from applicability of section 56(2)(x) has been provided to certain transfers [which are exempt transfers under section 47] in the nature of amalgamation/demerger/business reorganisations, no such exemption in section 56(2)(x) has been provided to transfer of capital asset by holding company to its subsidiary company and vice-a versa [which is also an exempt transfer under section 47(iv) and section 47(v) of the Act].

Consequently, such transfer of capital asset (including shares) by holding company to its subsidiary company or vice-a-versa, without consideration or for a consideration which is less than FMV determined in accordance with Rule 11UA, by an amount exceeding Rs. 50,000, would be subjected to tax as 'Income from other source" in the hands of the recipient.

Thus, despite the fact that transfer of capital asset by holding company to Indian subsidiary company and subsidiary company to Indian parent is not regarded as 'transfer' under section 47(iv) and section 47(v) of the Act, the same would be subjected to tax in the hands of the recipient under section 56(2)(x) of the Act. This puts internal re-organizations through non-amalgamation/demerger routes on an unequal footing and tends to promote amalgamation/ mergers over transfers and defeats the purpose of providing exemption to such internal re-organisations under section 47(iv) and section 47(v) of the Act and would result in tax implications in the hands of the transferee. Further, it may not always be feasible to do internal re-organisations through amalgamation/demerger route as this is time consuming and involves legal and other costs.

Further, the cost of acquisition of capital asset in the case of transfers covered within the provisions of section 47(iv) and section 47(v) [i.e. transfer of capital asset between holding company and subsidiary company], shall be the cost for which the previous

owner acquired the property. Thus, there would be an inconsistency between the provisions of section 47(iv) and section 47(v) read with section 49 which stipulate transfer at cost versus section 56(2)(x) which stipulates transfer at fair market value. Accordingly, by bringing the aforesaid transactions under the ambit of section 56(2)(x) would not serve any meaningful purpose and would be contrary to the provisions of section 47(iv) and (v).

- Section 50CA of the Act provides that the sale consideration for transfer of shares other than the quoted shares shall be deemed to be the fair market value; determined in accordance with the prescribed method, if the actual consideration is lower than such FMV. The term 'quoted share' is defined to mean "the share quoted on any recognized stock exchange with regularity from time to time, where the quotation of such share is based on current transaction made in the ordinary course of business". There is no clarity on the term 'regularity from time to time' used in the above definition.
- 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 infact 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.
- Currently property received by a trust which is created solely for the benefit of the relative of the individual does not fall within the ambit of section 56(2)(x). There is no clarity with respect to taxability under section 56(2)(x) in a case where trust is created solely for the benefit of the transferor and his relatives.
- 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.
- It is submitted that there should be a specific carve out to the effect that the exclusion list under section 56(2)(x) of the Act should also be widened to include any receipt of property by an assessee under the IBC framework in accordance with Resolution Plan as approved and administered by the NCLT. Similarly, provisions of section 50CA of the Act should not be made applicable in the hands of the seller for transactions pertaining to transfer of shares which are consummated under the IBC framework in accordance with Resolution Plan as approved and administered by the NCLT. The aforesaid carve outs are also warranted because the entire proceedings under the IBC are conducted through a transparent process with sufficient regulatory oversight as that of NCLT and, hence, they do not fall within the mischief which is sought to be curbed by provisions of section 56(2)(x) and 50CA of the Act.

  Granting of above tax reliefs/concessions will ensure participation of serious resolution applicants which will be in the best interests of all stakeholders. The Resolution Plans approved after factoring in these reliefs/concessions will result in quick revival of assets, freeing up liquidity for banks for further lending, increased economic activity, job savings /creation, increased contribution to the exchequer and will have multiplier effect on the associated economy. The re-rating of assets post approved Resolution Plan will also improve balance sheets of the banks thereby lowering capital infusion requirement from the Government. Further, a quick and timely resolution to the stressed assets with positive outcome implemented in a transparent manner will improve India's "Doing Business" ranking thereby ensuring participation from global players and resultant capital inflows.

- It is suggested that section 56(2)(x) of the Act should be amended to exclude "transactions not regarded as transfer" covered in section 47 of the Act from its ambit.
- Without prejudice to above, it is suggested that an amendment should be made in Proviso to clause (x) of sub-section (2) to section 56 of the Act, to include 'transaction not regarded as transfer under clause (iv) and clause (v) of section 47' along with other transaction not regarded as transfer under clause [(i), (vi), (via), (viaa), (vib), (vic), (vica), (vicb), (vid), (vii) of section 47) of the Act.

  Further, as mentioned above, the cost of acquisition of capital asset in the case of transfers covered within the provisions of section 47(iv) and section 47(v) [i.e. transfer of capital asset between holding company and subsidiary company], shall be the cost for which the previous owner acquired the property. Accordingly, there should be no loss to the revenue as well, where these transactions are kept out of the ambit of section 56(2)(x) of the Act.

  It is accordingly suggested that the aforesaid recommendation be considered suitably and necessary clarification be issued in the larger interest of industry and trade.
- Sections 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 suggested that a suitable amendment be made to exclude receipt by the trust created/established for the benefit of individual and/or his relatives from the ambit of section 56(2)(x) of the Act.
- 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 suggested that clarification be provided in section 50CA of the Act to determine the trading regularity of shares.

4.21.9. Final rules relating to valuation of unquoted equity shares for the purpose of section 50CA and section 56(2)(x) of the Act

The Final 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 Final 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.

4.21.10. Transfer of Capital Asset between Holding Company and Subsidiary –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.

4.21.11. Non-Compliance of conditions applicable to certain Re-organizations - Section 47

Issues

- Section 47A(1) of the Act provides that in case holding company does not continue to hold 100% of shares of the subsidiary company or converts/treats the transferred asset as stock-in-trade, within a period of 8 years from the date of the transfer of capital asset, the gains exempted under Section 47(iv)/ (v) of the Act shall be taxable in the hands of the transferor company in the year of transfer. It shall be noted that a period of 8 years is too long.
- Further, in any case such income should be taxable in the year of event specified in the Section and not in the year of transfer of capital asset.

Recommendations

- Section 47A (1) of the Act should be amended to reduce "period of 8 years" to reasonable period.
- Further, in any case, such income should be taxable in the year of event specified in the section and not in the year of transfer of capital asset.

- Words 'profits & gains' in Section 47A(1) of the Act should be replaced with the word 'income'.

4.21.12. 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 on ground situation is that 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:-
  - 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.

4.21.13. Tax Neutrality in case of Overseas Reorganization

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:-
  - 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.

Recommendation

- 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.

4.21.14. Continuation of Deduction under Section 80-IA in case of Re-organization

Issues

- Section 80-IA of the Act provides deduction in relation to profits of certain undertakings. It was well settled that in the case of restructuring of any entity owning such undertaking, the benefits of deduction will be available to entity owning the undertaking post restructuring.
- Board Circular Letter F.No. 15/5/63-IT (AI), dated 13th December, 1963 specifically provided that in the year of corporate restructuring, the benefit shall be available to transferor entity up to the date of transfer and to the transferee entity for the remaining period of tax holiday.
- Sub-Section (12) provided that in the year of restructuring deduction will not be allowable to the transferor entity but same will be allowed to the transferee entity as it would have been allowed, had the restructuring not taken place. In totality, this will restrict the total period of deduction to not more than the total period for which the deduction should have been allowed under the provisions of the Act.
- However, sub-Section (12A) was inserted in Section 80-IA with effect from 1st April, 2008 to provide that nothing contained in sub-Section (12) shall apply to reorganization post 1st April, 2007. A view is expressed that post insertion of sub Section (12A), benefit of deduction under Section 80-IA of the Act will not be available to the amalgamated/ resulting entity.

Recommendations

- Section 80-IA(12A) of the Act be deleted to enable restructuring of eligible entities.
- Section 80-IA(12) of the Act should be amended to provide for allowing deduction to the amalgamating/ demerged entity for the period till transfer date and to the amalgamated/ resulting entity post transfer.

4.22. Capital Gains

4.22.1. Issues under Section 54EC of the Act

Issues

- Section 54EC of the Act provides tax exemption on capital gains arising from the transfer of a long term capital asset, if invested in long-term specified assets within a period of six months from the date of such transfer. The investments in such bonds, in a FY and the subsequent FY, should not exceed Rs. 50 lakhs.
- Further, there might be a situation where, the specified assets are not available during the said period of six months. Also, it may be possible that the price/ rate/ cost at which the specified asset is available during the stipulated period may not be viable for the taxpayer to invest.
- Purpose behind granting of exemption is to promote investment in specified assets. There does not seem to be any rationale behind prescribing the monetary limit of Rs. 50 lakhs per investor or specifying the stringent time line of 6 months. Especially in the context that such funds would in any case be used for meeting the infrastructure requirements.
- The specified assets for the purpose of section 54EC are only bonds issued by National Highways Authority of India or by Rural Electrification Corporation Limited or any other bond notified by the Central Government. The Government should also include 'mutual fund units' within the purview of specified assets to channelize more investments in the capital markets.

Recommendations

- Currently, huge amounts are required to be deployed in the infrastructure sector to give the sector the much needed boost and this vehicle could be used for raising such infrastructure development funds. Thus, there is a need to revisit the limits prescribed.
- Moreover, the interest income on such bonds, which are presently fully taxable, should be awarded 'non-taxable' status.
- Proviso to Section 54EC(1) of the Act which restricts the investment in such bonds not exceeding Rs. 50 lakhs in a FY should be deleted.
- Recently inserted Second Proviso to Section 54EC(1) of the Act should also be deleted which restricts the investment in the FY of transfer and its subsequent FY, with respect to the asset transferred, in such bonds not exceeding Rs. 50 lakhs.
- The time period of 6 months should be liberalized and the exemption should be permitted for the investments made before the due date of filing of return of income under Section 139(1) of the Act.
- The list of specified assets should be broadened by including mutual fund units redeemable after three years.

4.22.2. Rate of Tax Applicable to Short-Term Capital Gains - Section 111A

Issues

- Section 111A of the Act provides that short-term capital gains on sale of shares of listed companies or units of equity oriented fund should be taxed at 15%. The rate was 10% till 31 March 2009.
- The difference between normal income and capital gain arising on transfer of assets is well recognized even under the Act. It is a known fact that owner of an asset incurs a lot of expenditure for maintaining an asset. In case such asset is used in business, deduction is allowed for such maintenance and other expenses. However, no such deduction is allowed if such asset is a non-business asset. Thus, it makes a strong case that rate of tax in case of capital gains should be different from the rate applicable to other incomes. This distinction is recognized to some extent in Section 111A and 112 of the Act. However, for short term gains on assets other than listed shares, such difference is not recognized.

Recommendations

- The rate for listed shares should be restored to 10% as was the position till 31st March 2009.
- Section 111A of the Act should be amended to provide the rate of tax for short term gain on transfer of assets other than listed shares to be at 20%.

4.22.3. Insertion of Section 50D in the Act

Section 50D is inserted to provide that in cases involving transfer of assets, if the consideration is not determinable, fair value of the consideration received or accruing shall be deemed to be consideration.

Issues

- Method of determining fair value is not specified under the Act.
- Section overlaps with certain other Sections providing similar mechanism for determining consideration, e.g. Section 45(3) dealing with transfer of a capital asset.

Recommendation

- Method for determination of fair value should be specified under the Act. Applicability of Section 50D of the Act should be restricted to the transactions not covered under other similar provisions.

4.23. Transfer Pricing

4.23.1. 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

(a) 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.

(b) 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 above, the threshold of interest expenditure for applicability of this section should be increased to at least Rs. 15 crores.

(c) Interest limitation rules are in nascent stage in India, therefore companies must be provided transition window to re-align its debt structure. Further, aligning the capital structure is time consuming and requires regulatory approvals. EBITDA capping should be initially @ 60-70% and phased reduction of the same to 30% could be provided over a span of three years.

(d) 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.

(e) 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.

(f) 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.

(g) 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.

(h) 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".

(i) 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.

(j) Sub section 1 of Section 94B of the Act specifically requires the lending to be from a non-resident associated enterprise for the section to trigger. However, branches or permanent establishments of foreign banks are also "non-residents" for the purposes of the Income-tax Act. Whilst branches or permanent establishments of foreign banks operate essentially as Indian companies and compete directly with Indian banks, debt by related Indian branches of banks or guarantees given by AEs towards borrowings by Indian companies from branches or permanent establishments of foreign banks would qualify for disallowance under the above provision. This places the Indian branches of foreign banks at a disadvantageous position vis-à-vis competing Indian banks.

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 threshold of interest expenditure for applicability of this section should be

increased to at least 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.
- 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 borrowings by Indian companies from Indian branches or permanent establishments of foreign banks should be wholly excluded from the purview of the section 94B (either by way of direct borrowing from or by way of guarantee by AE to such branches or permanent establishments of foreign banks).
- 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.

4.23.2. Introduction of secondary adjustment (Section 92CE)

The Finance Act, 2017 has introduced the concept of secondary adjustment on transfer pricing (TP) adjustments. A taxpayer is required to make a secondary adjustment, where the primary adjustment to transfer price has been made in the following situations:-

- *Suo moto* by the taxpayer in the return of income;
- By the Assessing Officer (AO) during assessment proceedings, and has been accepted by the taxpayer;
- Adjustment determined by an Advance Pricing Agreement entered into by the taxpayer;
- Adjustment made as per the Indian safe harbour rules; or
- Adjustment arising as a result of resolution of an assessment by way of the mutual agreement procedure under an agreement entered into for avoidance of double taxation.

'Secondary adjustment' has been explained as an adjustment in the books of account of the taxpayer and its associated enterprise (AE) to reflect that the actual allocation of profits between the taxpayer and its AE are consistent with the arm's length price as may be determined under one of the above five situations.

The additional amount receivable from the AE as a result of the primary adjustment should be repatriated by the taxpayer into India within a prescribed time limit. If the same is not received by the taxpayer within the time-limit, then the primary adjustment will be deemed as an advance extended to the overseas AE and a secondary adjustment in the form of notional interest on the outstanding amount would be subjected to tax as an income of the taxpayer.

The above requirements for repatriating the amount of TP adjustment into India and imputing a notional interest, are triggered if the primary TP adjustment exceeds Rs. one crore. The time limit for repatriation and manner of computation of interest has been prescribed by CBDT vide Notification No. 52/2017, dated 15 June 2017.

Issues

- The additional amount receivable from the AE as a result of the primary adjustment should be repatriated by the taxpayer into India within 90 days from the due date of filing return of income under section 139(1) of the Act or from the date of the order of AO or the appellate authority, as the case may be (in situation 2 mentioned above). If the same is not received by the taxpayer within 90 days, then a notional interest on the outstanding amount receivable from the AE (deemed as an advance) should also be offered to tax as an income of the taxpayer.

  The above requirement for repatriating the adjustment amount into India and imputing a notional interest are triggered if the primary adjustment exceeds Rs. one crore and pertains to only primary adjustments made in respect of FY 2016-17 and subsequent years.

The Indian regulations under section 92CE of the Act on secondary adjustment require the taxpayer and the AE to make adjustment in the books of account. However, the books of account of taxpayer and its overseas AE would be closed by the time such an adjustment is determined and it would not be practically possible to record it in the books of the relevant financial year. Also, it may not be within the control of the taxpayer to enforce recording of an adjustment in the books of accounts of the AE. Moreover, it would be beyond the jurisdiction of the Indian regulations to mandate such an action on part of the AE located outside of India.

- The delay in repatriation may arise due to reasons not attributable to taxpayer i.e. on account of application of other legal and regulatory requirements such as application of exchange control regulations, Goods and Services Tax, customs regulations and applicability of thin capitalisation rules in the tax jurisdiction of the AE. If the deemed loan cannot be repaid by the non-resident AE to the Indian taxpayer, due to commercial, legal or regulatory issues, the loan would remain in existence indefinitely, leading to notional interest imputations.

  Making an accounting entry may have an impact on 'Book Profit' for calculations under section 115JB of the Act in the year of passing of such entry and may have some further implications if the taxpayer's Minimum Alternate Tax (MAT) liability exceeds the computation under normal tax provisions.

- The phrase "secondary adjustment" has been defined in clause (v) of Sub-section (3) of section 92CE of the Act to mean an adjustment in the books of account of the assesse and its associated enterprise to reflect that the actual allocation of profits between the assessee and its associated enterprise are consistent with the transfer price as determined as a result of primary adjustment, thereby removing the imbalance between cash account and actual profit of the assessee. Sub-section (2) lays down the requirement for excess monies to be repatriated to India and for interest to be levied thereon, if not repatriated within the prescribed time. However, sub-section (2) does not refer to 'secondary adjustment' as envisaged under Sub-section (1) and defined in Clause (v) of Sub-section (3). The absence of references to sub-section (1) and/or 'secondary adjustment' in Subsection (2) results in an apparent disconnect between Sub-sections (1) and (2) which may have unintended consequences.

- In case interest imputed is not paid in the year of imputation, it is unclear as to whether it will take the colour of a "primary adjustment" and interest will be levied on such unpaid interest of last year (treating it as an advance). This will lead to a cascading effect and unnecessary burden on the assessee.

- The provisions, as presently worded, may give rise to an interpretation that even where the primary adjustment is made in the hands of non-resident, secondary adjustment follows. As a consequence, it may be interpreted as allowing repatriation of funds outside India, which may not be permitted even in terms of FEMA/RBI regulations.

- Section 92CE of the Act deems the difference between the transaction price and arm's length price as an advance (which is to be recorded in the books) and provides for

imputation of interest on such advances. However, there is no specific provision to reverse the advances appearing in the books even in case where the AE relationship ceases to exist or in case where the excess money is repatriated.

Recommendations

- Sub-Sections (1), (2) and (3) of section 92CE of the Act need to be revisited to streamline and appropriately link up the three sub-sections to provide adequate clarity as to the specific requirements from the taxpayers.
- Further, bilateral APAs and MAPs shall be excluded from the purview of the section 92CE of the Act since the terms of bringing money into India would already have been decided by the competent authorities of the two countries and such terms should prevail over a domestic law. It should be further clarified that the APA signed prior to insertion of section 92CE of Act should not be covered by the secondary adjustment provisions.
- The computation mechanism for levy of interest under Sub Section (2) should be clearly prescribed with detailed examples to obviate uncertainty including the trigger for such secondary adjustment or interest levy and the start date for levy of interest. Appropriate safeguards by way of clarificatory provisions/Rules should be brought in to obviate an interest on interest situation and cascading effect.
- Necessary clarifications on accounting treatment and adjustment in books of accounts of the AE to be provided. Clarifications are also sought in cases where delay in repatriation is due to reasons not attributable to taxpayer.
- It is unclear as to how the secondary adjustment will be allocated where transactions are with Multiple AEs and are benchmarked using overall Transaction Net Margin Method (TNMM) on an aggregated basis. Clarification is requested to explain the basis on which the quantum of secondary adjustment can be distributed to different AEs for adjustment made to the overall net margin of the taxpayer w.r.t. multiple AEs/ transactions.
- A clarification is required on whether the secondary transaction in the form of interest would be included for MAT purposes.
- The Government should clarify the term 'has been accepted by the taxpayer' in order to provide certainty on the applicability of these provisions in situations e.g. where the taxpayer is in appeal against the assessment order to Tribunal, whether will secondary adjustment provisions be applicable only after the Tribunal proceedings are completed or the same will become applicable after Court proceedings are completed, i.e. what happens if the taxpayer further appeals to High Court/Supreme Court. Further, there could be situations where the assessee may not have appealed against the primary adjustment considering the cost of litigation vis-à-vis the quantum of primary adjustment. It is suggested that no secondary adjustment should be made in such cases and suitable amendment be made in the provisions of section 92CE of the Act.
- Clarifications are requested for cases where the AE ceases to exist i.e. AE has been liquidated. Also, clarification may be provided for a scenario, where if at the time of

making secondary adjustment, the AE relationship ceases to exist.

- It is recommended that section 92CE(2) of the Act be amended to clarify that the section applies only in case where the primary adjustment is made in the hands of the Indian AE.
- Under regulations of few other countries like South Africa, draft regulations in UK, inter-company setting off of accounts is allowed for deemed loans arising out of secondary adjustments provisions, however the same has not been provided for under Indian regulations, which make the Indian regulations more onerous. Permitting such netting off may ensure that the outstanding loan balances do not remain so till perpetuity and the interest on the same does not keep accumulating endlessly.
- It may be specifically provided that the advances appearing in the books of the parties be reversed in cases where AE relationship ceases to exist or excess money is repatriated.
- Clarity should also be provided with regard to non-applicability of provisions of section 2(22)(e) of the Act where any sum is treated as an "advance" by virtue of the secondary adjustment.

4.23.3. 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.

4.23.4. 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.

4.23.5. 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.

4.23.6. Specified Domestic Transaction

'Specified Domestic Transactions' (SDT) is covered under Transfer Pricing provisions if the aggregate amount of all such transactions entered by the taxpayer in the previous year exceeds Rs. 20 crores (w.e.f FY 2015-16, before that it was Rs. 5 crores). Further, the applicability of domestic transfer pricing provisions is restricted to entities with tax holiday units from FY 2016-17.

Recommendations

- The words "close connection" appearing in Section 80-IA (10) needs to be clarified to avoid ambiguity in the application of provisions of Section 92BA of the Act.

- Further, clarity should be provided with regard to inter-unit allocation of costs between eligible and non-eligible units i.e. whether corporate cost allocations from a non-tax holiday unit of a company to a tax holiday unit of the same company would get covered within the provisions of Section 80-IA(8) of the Act and consequently need to be reported as a specified domestic transaction.
- The Advance pricing agreement provisions are applicable to only international transactions. The same should also be made applicable to domestic transactions covered by transfer pricing regulations.

4.23.7. Safe Harbour Rules

The Safe Harbour Rules (SHRs) have been revised in 2017. Under the revised SHRs, safe harbour ratios were rationalised, safe harbour for receipt of low value adding intra group services (LVIGS) was introduced, upper turnover threshold of INR 200 crore introduced for all contract service providers [IT, ITeS, KPO, R&D for IT and generic pharmaceutical drugs], safe harbour rates on loans advanced in foreign currency have also been introduced. Most of these revisions are welcome, however, there are still some issues in the SHRs that need to be addressed and are given below:-

Issues and Recommendations

The definitions of various eligible international transactions under the SHRs like KPO services vis-a-vis ITeS, Software development services vis-à-vis contract R&D services relating to software development, leave a lot of room for subjective interpretations and there is lack of clarity on categorization or classification of these services. Clear and more objective criterions may be introduced for classification of services. For e.g., the artificial barrier between contract IT services simpliciter and contract IT R&D services should be removed to have one uniform rate for all contract IT services.

The prescribed safe harbour rates for outbound loans are otherwise fair, yet the obligation of having the credit rating of the overseas borrower being approved by CRISIL, is an additional cost burden for taxpayers who wish to opt for the SHRs. Thus, it is suggested that the requirement of credit rating of the overseas borrower to be approved by CRISIL should be removed.

Further, the arm's length prices or ratios prescribed under the SHRs should be rationalised for manufacturers of auto components, to make the same attractive enough for such taxpayers to opt for the SHRs.

4.23.8. 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.

4.23.9. Filing of Form 3CEB by Foreign Companies

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.

4.23.10. Allow appeal before Commissioner of Income tax (Appeals) against order of penalty under section 271AA

Issue

Section 271AA of the Act provides that (without prejudice to the provisions of section 270A or section 271 and 271BA), if a person in respect of an international transaction/specified domestic transaction

- Fails to keep and maintain any such information and document as required by sub-section (1) or sub-section (2) of section 92D;
- fails to report such transaction which he is required to do so; or
- maintains or furnishes an incorrect information or document,

the Assessing Officer or Commissioner (Appeals) may direct that such person shall pay, by way of penalty, a sum equal to 2% of the value of each international transaction or specified domestic transaction entered into by such person.

It may be noted that there is no mechanism under the provisions of the Act to allow filing of appeal before the Commissioner (Appeals) against the order passed by the Assessing Officer imposing the above mentioned penalty.

Recommendation

It is suggested that the provisions of section 246A of the Act be amended to allow the taxpayer to file an appeal before the Commissioner of Income Tax (Appeals) against the aforesaid penalty order passed by the assessing officer.

4.24. Financial Services

4.24.1. Income Characterization – Capital Gains vs. Business Income

Issue

- The Finance Act 2014 amended the definition of capital asset under Section 2(14) of the Act to include securities held by Foreign Portfolio Investors ('FPI')/Foreign Institutional Investors ('FII'). Therefore, the gains earned by FPIs/FIIs from securities transactions are characterized as capital gains. It may be noted that Alternative Investment Funds ('AIFs'), Venture Capital Funds ('VCFs') and Foreign Venture Capital Investors ('FVCIs') make and hold investments in portfolio companies with an objective of long term capital appreciation. At times, depending on the capital needs of the promoters and the philosophy/investment strategy of the AIFs/VCF/FVCI, they may end up acquiring stakes which may be in excess of 20% and may even exceed 51%. Notwithstanding their stake in the investee companies, the objective of the AIFs/VCF/FVCI is to merely provide the financial capital to the investee companies.

Recommendation

- Therefore, the income arising from transfer of securities held by AIFs/VCFs/FVCIs be clearly spelled out to be capital gains. The provisions of the Act should be suitably amended to explicitly provide that income from sale of investments by AIFs/VCFs/FVCIs would be treated as 'capital gains'. This will provide much needed clarity and mitigate avoidable litigation with the tax authorities on characterisation issues.

4.24.2. Extension of Tax pass through to Category III Alternative Investment Funds ('AIFs')

Issue

AIFs are vehicles set-up to pool investments from various investors and to invest across different asset classes using different investment strategies. In real terms, the income that is sought to be taxed is the income of the investors. The taxation of an income, or the taxpayer itself, should not change, merely because an investor decides to use a professional asset manager to make investment decisions for him vis-à-vis directly making those investment decisions. Further, the manner of taxation should not also change, where an investor invests in an AIF instead of investing in his own name using a SEBI registered

portfolio manager. The tax rules applicable to 'investment funds' in Chapter XII-FB of the Act should be extended to close ended Category III AIFs with suitable modifications to eliminate the distinction between the tax treatment of business income and income under other heads of income in the hands of the AIF/its investors. Category III AIF's are also regulated under the Securities and Exchange Board of India (Alternative Investment Fund) Regulations, 2012 made under the Securities Exchange Board of India Act, 1992 along-with Category I & II AIF's. Category III AIFs introduced a product that was hitherto not available in the Indian financial sector. A clear tax code for taxation of such AIFs based on the pass through tax principle will be critical for the success of this product in the medium to long-term.

Recommendation

It is recommended to include Category III AIF's under the provisions of section 115UB in order to provide clarity on taxation of Category III funds.

4.24.3. International Financial Services Centre

The Finance Act, 2016 made various amendments in the Act with a view to incentivise the growth of International Financial Services centres into a world class financial services hub. However, certain issues which still need to be addressed to provide a competitive tax regime to Indian IFSC are given below for consideration of the Government:-

Issues

- Section 115JB(7) of the Act states that where the assessee is a unit located in an IFSC and derives income solely in convertible foreign exchange, a lower MAT rate of 9% shall apply as compared to the present MAT rate of 18.5%. The current MAT rate of 9% does not make the Indian IFSC globally competitive.
- Section 115-O(8) of the Act states that no tax on distributed profits will be charged in respect of the total income of a unit in an IFSC that derives income solely in foreign exchange on any amounts declared, distributed or paid as dividends (interim or otherwise) out of its current income on or after 1 April 2017**.** Although the Memorandum Explaining the provisions of the Finance Bill 2016 states that the amount of dividend on which DDT is not leviable by virtue of section 115-O(8) is exempt in the hands of the person receiving the dividend, there is some ambiguity as section 10(34) has not been consequentially amended to exempt the income in the hands of the shareholder.
- Mutual funds are permitted to operate in an IFSC. However, additional income-tax on income distributed by mutual funds has not been waived on the same footing as dividend distribution tax.
- Several of the tax exemptions for units located in an IFSC are tied to the condition that income is derived solely in convertible foreign exchange. Income earned from shares of domestic companies may not be received in convertible foreign exchange. Portfolio Managers, Alternate Investment Funds and Mutual funds are permitted to invest in shares of domestic companies vide SEBI Circular No. SEBI/HO/MRD/ DSA/CIR/P/2017/45 dated May 23, 2017.

- Tax holiday under section 80LA of the Act inter alia mentions that deduction from gross total income shall be available in respect of income from any unit in the IFSC from its business for which it has been approved for setting up in such a centre in a Special Economic Zone. There is some ambiguity as regards FPIs as they earn income in the nature of capital gains, they do not set up a unit in an IFSC and they do not engage in business. As per SEBI(IFSC) Guidelines 2015, SEBI registered FPIs can operate in an IFSC without any additional documentation or prior approval process. Further, the tax holiday period of ten years under section 80LA of the Act is very short when compared to tax breaks provided globally e.g. Dubai Offshore Financial Centre provides a tax break for 50 years.

Recommendations

- It is suggested that MAT should be abolished for a unit located in an IFSC to compete with tax breaks offered by IFSCs globally (e.g. Dubai (0%), Malaysia (3%).
- It is suggested that section 10(34) of the Act be amended to specifically clarify that dividend income is exempt in the hands of the shareholder even though the company has not paid DDT by virtue of section 115-O(8) of the Act.
- It is suggested that the provisions of Chapter XII-E of the Act may be amended to waive additional income-tax on income distributed by mutual funds operating in an IFSC.
- A carve out may be made in respect of availability of exemptions to a unit located in an IFSC if the sole reason for deriving income other than in convertible foreign exchange is on account of investing in shares of domestic companies.
- It is suggested that it may be suitably clarified that given the nature of the industry in which Foreign Portfolio Investors operate, tax holiday under section 80LA of the Act will be available to FPIs, although the income earned is in the nature of capital gains and a unit is not set up in an IFSC.
- It is suggested that the tax holiday period for unit in IFSCs may be suitably increased.

4.24.4. Taxation regime for Infrastructure Investment Trust and Real Estate Investment Trust (Business Trust)

4.24.4.1. Definition of equity oriented fund

"Equity oriented fund" as defined under Act is a fund which has been set up as a mutual fund in terms of section 10(23D) of the IT Act and which invests more than 65% of the total investible funds in the equity shares of domestic companies. Long term capital gains arising from transfer of unit of an equity oriented fund are exempt from tax.

In accordance with the press release issued by SEBI on January 14, 2017, we understand that SEBI proposes to permit mutual funds to invest in the units of InvITs and REITs. Thus, in a case where the unitholder transfers a unit of a mutual fund, which invests its proceeds in InvITs or REITs, such unitholder shall not be given the benefit of exemption from long term capital gains as the investment in InvITs or REITs is not covered within the definition of an equity oriented fund.

The Memorandum to Finance (No. 2) Bill, 2014 stated that listed units of business trust would be given the same tax benefits in respect of taxability of capital gains, as equity shares. Further, units of business trusts, similar to equity shares, are subject to securities transaction tax. In view of the same, a mutual fund investing in the units of business trusts should be construed as investing in equity in order to satisfy the definition of an "equity oriented fund". However, the satisfaction of the present definition of an "equity oriented fund" requires investment of more than 65% of its investible surplus only in equity shares. Thus, in line with the Government's intention to promote business trusts, we respectfully submit that it would be important to amend the definition of an "equity oriented fund" to include investment in business trust units, to encourage such mutual funds to invest in the units of InvITs or REITs.

4.24.4.2. Period of holding

As per the existing provisions of section 2(42A) of the IT Act, a long-term capital asset means an asset which has been held for 36 months or more (other than certain assets where the period of holding for qualifying as long term capital asset is less). However, the period of holding to qualify for a long-term capital asset is 12 months in case of listed securities (other than units) and units of an equity oriented fund. The units of an Invite or REIT are currently not eligible for a lower period of holding to qualify as a long-term capital asset.

As stated above, the Memorandum to Finance (No. 2) Bill, 2014 provided that the units of a business trust would be treated at par with equity shares of a listed company. In view of the same, pursuant to the said Finance Bill, the exemption from long term capital gains under section 10(38) of the IT Act was extended to units of business trusts. Though the exemption

from long term capital gains has been extended in respect of capital gains arising to the holder of units of a business trust, section 2(42A) of the IT Act which deals with the period of holding has yet not been revised.

Even though the units of a business trust are listed, the unitholders of a business trust do not enjoy the benefit of lower period of holding, available to shareholders of a listed company or unitholders of an equity oriented fund. Therefore, in line with the intention of the Government evidenced by the proposal stated in the Memorandum to Finance (No. 2) Bill, 2014, we believe, that in order to promote investment in business trusts in India and provide impetus to the Indian capital market, the period of holding for units of a business trust to qualify as a long-term capital asset should be reduced to 12 months.

4.24.4.3. Dividend distribution tax for a multi-level structure

Currently, under the provisions of section 115-O of the Income Tax Act, 1961, any distribution of profits made by a domestic company, in which a business trust, being an InvIT or REIT, holds the whole of the nominal value of the equity capital (excluding the capital held by Government or Government body or capital mandatorily required to be held by any other person under any prescribed law or direction), shall not be subject to DDT. Accordingly, distribution of dividends by such a domestic company to a business trust is exempt from payment of DDT. In this regard, it may be pertinent to note that the SEBI regulations governing business trusts, classified a SPV as a company or limited liability

partnership that holds not less than 80% of its assets directly in properties and does not invest in other SPVs. In other words, multi-level structure was not permitted under the regulations issued by SEBI governing InvITs and REITs.

In the infrastructure sector, and more specifically in relation to a public-private partnership projects, bidders for such projects are required to create SPVs to develop the infrastructure asset. Typically, (i) in the ports sector, operators of ports incorporate separate SPVs below the entity that leases the port under the relevant concession agreements; (ii) in the roads infrastructure sector, concession agreements require the applicant to incorporate a separate SPV that will sign the concession agreement with the relevant authority and undertake the project; and (iii) in the transmission sector, bidders are required to specifically bid on behalf of SPVs which are created by the bid process co-ordinator in accordance with the requirements specified by the Ministry of Power, Government of India. Accordingly, SPVs are created below the HoldCo for the execution and maintenance of projects.

Based on representations and suggestions made by various market constituents, SEBI has facilitated the growth of InvITs and REITs, and issued amendments to the extant framework, permitting a multi-level structure under an InvIT or REIT, thereby allowing investment in one SPV through another SPV by a business trust subject to the fulfillment of specified conditions.

In view of the amendments issued by SEBI, business trusts may use multi-level SPV structures. As the Government has already, *vide* amendment to section 115-O of the Act introduced by Finance Act, 2016, agreed to grant exemption from payment of DDT on distribution made to a business trust to promote such alternate investment vehicles, we believe that the Government may, in light of the recent amendments, further amend section 115-O of the Act, to provide DDT exemption to any dividend distributed under such multi-level structure. In other words, an exemption from payment of DDT on any profits distributed by a subsidiary of the specified domestic company as defined under section 115-O of the Act, shall be provided.

4.25. Tax Deducted at Source (TDS)

4.25.1. TDS on Monthly and Year end provision entries in Books of Accounts

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. 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 unnecessary burden posed on the payer in carrying extensive reconciliations.

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. There are various tribunal judgements also to support this position. This will also go a long way towards ease of doing business and in reducing the litigation.

4.25.2. Introduction of a scheme for allowing self-declaration by a deductor for lower rate TDS

It has been observed that for obtaining certificate under section 197 of the Act, a taxpayer has to incur a lot of cost and efforts every year and the certificates are based on estimations only. Also, where are there are additional transactions entered or limit provided in the 197 certificate is exhausted during the year, a fresh application has to be filed and entire proceedings are undertaken again. To provide convenience to tax payers and to reduce costs and efforts of both taxpayers and the tax authorities, it is suggested the Government should introduce a scheme wherein the deductee may be given an option to furnish a self-declaration to the deductor for lower rate of TDS. The scheme should be optional and an assessee shall have the option to opt for other remedies under section 197 of the Act (issue of Nil or lower withholding certificate by the assessing officer) and 197A of the Act (furnishing of declaration, in Form 15H, by the recipient to the deductor that his income-tax liability is Nil. Minimum rate of 1% should be prescribed for tax deduction at source. Even if estimated income of the assessee justifies Nil TDS or TDS at rate lower than 1%, an assessee opting for this scheme shall furnish a declaration to the deductor authorising the deduction to deduct tax at the rate of 1%. Where an assessee opts for this scheme, the same TDS rate shall be applicable to all the income/ receipts payable by all the deductors, irrespective of the TDS section under which the payments would be covered. In other words, the assessee should be allowed to furnish the declaration with a single TDS rate for all types of income/receipts receivable from all the deductors. FICCI has also made a detailed representation in this regard to the Government and would be happy to participate in further discussions to take the matter forward.

4.25.3. TDS on prepaid distributor margins/discounts from telecom operators

It is a practice in the telecom industry to enter into an arrangement with the pre-paid distributors on “Principal to Principal” basis such that all material is supplied at a discount to the MRP and the distributor can, in turn, sell at any price up to the MSP (max selling price) of the product. The risk of any losses is not borne by the telecom operator but by the distributor. There has been continuous litigation on whether the relationship between the telos and distributors is on “Principal to Principal” or “Principal to Agent” basis. TDS is applicable only if the relationship is of principal to agent basis else not. It is strongly believed that issuance of a clarification that such discounts does not fall within the ambit of TDS

provisions is warranted. Alternatively, it is suggested that the Government should introduce the TDS rate of 1% on such payments, 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.

4.25.4. Concessional rate of 5% on income by way of interest from Indian company – Section 194LC

Issue

The concessional rate of withholding tax on interest as per section 194LC of the Act is applicable only in respect of monies borrowed under a loan agreement or by issue of long term bond (including long term infrastructure bond) before July 1, 2017. 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. One of the conditions prescribed in the circular 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.

Recommendation

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.

4.25.5. TDS on rent by individual and HUF – Section 194IB

The Finance Act, 2017 has inserted section 194IB of the Act to provide that individuals or HUF (other than those covered under section 44AB of the Act), to deduct tax at source @ 5% on payment of rent to a resident exceeding Rs. 50000 per month or part of month during the previous year.

Issues

- Applicability of the said provision would cause genuine difficulty for small persons. The said provision is likely to cause hardship to the middle class taxpayers, who have taken premises on rent for residential accommodation/carrying on business. It will unnecessarily burden them with additional compliance burden of deducting and deposit tax on rent paid. Further, it is also not clear as to how the said provision is to be applied for one time rent payment like hiring hall etc.

Recommendations

- The threshold of Rs. 50,000 per month should be increased to Rs. 1,00,000 per month and a higher threshold for one time payments needs to be provided for.
- Since purpose of this provision is to gather information about payee's receiving rent exceeding Rs.6 lakhs p.a, it is suggested, instead of bringing in TDS, a provision should be made to provide annual statement of information, whereby, payer provides information of payment of such rent made by them, along with name and PAN number of the person to whom payment is made.
- Without prejudice, this provision should not be made applicable if rent is paid by cheque and PAN of Payee is available and payee furnishes such information annually to tax office.

4.25.6. 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.

4.25.7. 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 deducted which contains TDS details of the deductee based on the TDS statement (e-TDS 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 AS-26 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 requested that CBDT may call for details of cases in which TDS credit has been denied on the basis that credit was available on the basis of 26AS but not on basis of data in department's system.

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.

Moreover, a taxpayer claims credit of TDS on the basis of TDS figures reflected in Form 26AS at the time of filing the return of income. In case TDS reflected in Form 26AS is enhanced owing to reasons such as update/revision of TDS returns by tax deductor etc. and the time limit for filing the revised return has expired, the tax payer is not able to claim the enhanced credit of TDS. The enhanced credit is not allowed by the tax officer during the time of assessment proceedings since the updated figure is not claimed in the return of income of the taxpayer. The tax payer is unable to claim the said enhanced TDS credit as the time limit for filing the revised return is already lapsed. Then the other option left with the taxpayer is:-

- Filing of rectification application - In case the relevant assessment has already been completed, the request for Form 26AS based increased TDS credit claim by way of rectification under section 154 is denied on the ground that the same has not been claimed in the revised return of income.
- Approach CBDT under section 119(2)(b) of the Act for the said claim – However as per Circular No. 9/2015 dated 9 June, 2015, the taxpayer has to forgo interest on eligible refunds under this section and hence not a suitable option for taxpayer.
- Further in a situation where intimation under Section 143(1) of the Act is issued subsequent to the filing of return of income, where no proper assessment proceedings have taken place, there is no mechanism for the taxpayer to make a claim for TDS credit.

It is requested that instructions should be issued to the field officers to accept Form 26AS based TDS credit claims during assessment proceedings (or even after completion of assessment proceedings), subject to the only condition that the taxpayer furnishes evidence that the corresponding income had been shown in the income tax return.

It is further suggested that instructions should also be issued for processing of rectification application filed by the taxpayer under section 154 of the Act for revising its claim for credit of TDS as per updated Form 26AS.

4.25.8. 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.

4.25.9. Clarity on TDS on Export Commission Paid to Non-Resident Agents

Issue

Central Board of Direct Taxes ('CBDT') had issued Circular no. 23 dated 23 July 1969, clarifying that commission paid to non-resident agents during the course of export was not taxable in India. Further, vide circular no. 786 dated 7 February 2000, the CBDT had again stated that, such commission paid to non-resident agents was not taxable in India under section 5(2) and 9 of the Income Tax Act, 1961 ('the Act') and no tax is therefore deductible under section 195 of the Act.

CBDT vide Circular No. 7/2009 dated 22 October, 2009 withdrew the circulars No 23 dated 23rd July, 1969, No. 163 dated 29th May, 1975 and No. 786 dated 7th February, 2000. The reason stated by CBDT in its 2009 circular was that the circular cannot be interpreted to allow relief to the taxpayer who is not in accordance with the provisions of section 9 of the Income-tax Act or with the intention behind the issue of the Circular. The 2009 circular also stated that it has been noticed that interpretation of the Circular by some of the taxpayers to claim relief is not in accordance with the provisions of section 9 of the Income-tax Act, 1961 or the intention behind the issuance of the Circular.

Even if the aforesaid Circulars have been withdrawn, the legal position with respect to the taxability of the commission paid to foreign agents has not changed in view of section 9 of the Act and judicial pronouncements are in favour of the taxpayers. The Hon'ble Supreme Court in the case of CIT v. Toshoku Limited (1980) (125 ITR 525)(SC) has held that considering the statutory provisions of the Act, the commission amounts which were earned by the non-resident for services rendered outside India cannot be deemed to be income which has either accrued or arisen in India. It was also held that the non-resident agent did not carry on any business operations in the taxable territories as contemplated by Explanation 1(a) to Section 9(1)(i) of the Act. The position has been reaffirmed by the various courts that even after the withdrawal of circular no. 23 (supra), the commission paid to non-resident is not liable to tax under the Act when the services were rendered outside India, services were used outside India, payments were made outside India and there was no business connection of the non-resident in India.

Even assuming that the non-resident agent has a business connection in India, as no operations, per se, are carried out by him in India, as per Explanation 1(a) to section 9(1)(i) of the Act, no income can be attributed in India and hence taxed in India. This principle has been affirmed by the Hon'ble Supreme Court in the case of Carborandum vs CIT (108 ITR 335) as well as in the case of Toshoku Ltd (supra).

However, by withdrawal of circular no. 23 (supra), the commission paid to non-resident agents for the purpose of export is being perceived by the tax authorities as taxable in India in virtually all the cases. The tax officers are not giving cognizance to the facts of the cases and judicial precedents relied upon by the taxpayers. Consequently, a large number of Indian companies are facing the issue of disallowance of the expense in respect of the said commission and have been served notices with huge demands for failure to deduct tax at source on the commission paid to its foreign agents.

The arbitrary disallowance of the export commission by the tax officers in the hands of the Indian company has created widespread litigation. This is gravely affecting the cash flow of the companies and is acting as a hindrance for the Indian companies to develop their market internationally.

Recommendation

It is recommended that it should be clarified that the commission payment to non-resident agents is not taxable in India if they does not fall within the purview of section 5 and section 9 of the Act. It should be further clarified that the tax withholding obligation in the hands of the payer would not arise if the commission is not chargeable to tax under the Act, irrespective of whether a specified declaration from the revenue authorities, under section 195 of the Act, has been obtained or not.

4.25.10. 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.

4.25.11. Enhancement of Limits for TDS - Section 194C and others

Issues

- Under Section 194C of the Act, TDS is applicable in respect of contracts for manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from such customer. However, in a large number of instances, it is observed that the material which is purchased from the customer represents a small fraction of the total cost and this provision has created huge operating problems, since the transaction may be a 'principal–to principal' contract for purchase and sale of goods and the profit margin may be very small.
- Currently, any payment for contract services rendered which exceeds Rs. 30,000 at a time or Rs. 100,000 per annum requires the person responsible for making such payments to deduct tax at source under Section 194C of the Act.

Recommendations

- It is suggested that the provisions of Section 194C of the Act be should be applicable only in such cases where the material purchased from the customer is substantial in nature, i.e., say it exceeds 40% of the total material cost (inclusive of raw materials and packing materials).
- It is recommended that the threshold limit should be increased to Rs. 50,000 for single payment under Section 194C of the Act.
- On similar basis, considering the inflation quotient, the threshold limits for other TDS provisions should also be enhanced as follows:-

Section	Category	Enhancement requested
194A	Interest on Bank Deposits	TDS limit of existing Rs.10,000 to be increased to Rs.1.00 Lakhs since the basic exemption limit of Income increased substantially and the senior citizens are affected in this category.
194I	Payment of	The existing limit of Rs.1.80 Lakhs per year to be

	rent	enhanced to Rs.3.00 Lakhs.
194J	Payment to Professionals	The existing limit of Rs.30,000 to be enhanced to Rs.1.00 Lakhs

4.25.12. 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.

Recommendations

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.

4.26. Personal Tax

4.26.1. 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.
- In this connection, what has not been appreciated is that many stock options come with a rider that employees cannot sell/transfer the shares exercised by them under Employee Stock Option Plan ('ESOP') for a particular period. This is primarily intended to retain the employees from leaving the employment once the options are exercised. Ownership of the property carries with it certain basic rights, such as a right to have the title to the property, a right to possess and enjoy it to the exclusion of everyone else, and a right to alienate it without being dictated to. The employees do not have economic freedom with respect to such shares.
- ESOP shares stand on a different footing because on the date of exercise, the shares are subject to lock-in condition and cannot be considered to be a benefit and therefore, ought not to be fictionally treated as benefit and brought under the ambit of perquisites

for taxation purposes. Section 17(2)(vi) of the Act seeks to tax a notional benefit when the actual gain is not even realized by the employee, and is not certain either. It is possible that the actual sale of shares could result in a loss for the employee. Since tax paid earlier cannot be set off against the capital loss, the employee suffers a double loss, namely tax outgo and loss on sale of shares.

The Supreme Court, in CIT v. Infosys Technologies Ltd., [2008] 2 SCC 272, at page 277, had aptly held:

> *"During the said period, the said shares had no realisable value, hence, there was no cash inflow to the employees on account of mere exercise of options. On the date when the options were exercised, it was not possible for the employees to foresee the future market value of the shares. Therefore, in our view, the benefit, if any, which arose on the date when the option stood exercised was only a notional benefit whose value was unascertainable. Therefore, in our view, the Department had erred in treating Rs. 165 crores as perquisite value being the difference in the market value of shares on the date of exercise of option and the total amount paid by the employees consequent upon exercise of the said options."*

- It may be mentioned that only when Fringe Benefit Tax (FBT) was introduced by the Finance Act 2005, these provisions were changed for the purposes of taxation of ESOPs under FBT regime. Unfortunately, those very provisions have now been brought back by way of insertion in sub-clause (vi) of sub-Section (2) of Section 17 of the Act, after the abolition of FBT, which has caused a lot of anxiety. It is imperative that the earlier tax treatment be restored to facilitate the employers in retaining talented persons in the organization.

Recommendation

- It is suggested that ESOPs should not be subject to tax on notional perquisite value and taxed only on capital gains arising from the sale of shares, as was the position till 31st March 2006.

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.

4.26.2. Taxation of National Pension Scheme

Currently, the National Pension Scheme (NPS) works on Exempt, Exempt, Tax (EET) regime whereby the monthly/periodic contributions during the pension accumulation phase are allowed as deduction and the returns generated on these contributions during the accumulation phase are also exempt from tax, however, the terminal benefits on exit or superannuation, in the form of lump sum withdrawals, are partially taxable in the hands of the taxpayer in the year of receipt of such amount. An amendment was introduced by Finance Act, 2016, wherein forty percent of the accumulated corpus upon withdrawal/ superannuation was made tax-free whilst balance corpus of sixty percent continues to be taxable.

Issue

- In order to encourage taxpayers to make voluntary higher contributions towards NPS, it should be made more tax-friendly as the objective of this scheme is to create a pensionable society. Accordingly, the tax regime of NPS should be made Exempt, Exempt, Exempt (EEE) from the current EET regime on the lines of other retirement schemes like Employee Provident Fund and Public Provident Fund.
- Without prejudice to above, the benefit of 40% exemption for withdrawal from National Pension Scheme (NPS) by any employee be extended to withdrawals by any person and not just employees. It is suggested the sub-section (12A) of section 10 of the Act providing for exemption of 40% of payment from NPS Trust to “an employee” on closure of account or opting out of pension scheme, may be modified to allow such exemption to payment from the NPS Trust to “an individual”, since exemption under the said clause is available in respect of withdrawals from NPS by self-employed individuals also.

4.26.3. Taxation of contribution to Superannuation Fund in excess of Rs. 1.5 lakh - Section 17

Issues

- Section 17(2)(vii) amended by the Finance Act, 2016 provides that the amount of any contribution to any approved superannuation fund by the employer in excess of Rs. 1.5 lakh will be taxable as perquisite in the hands of the employee.
- It has to be appreciated that contributions to superannuation fund may or may not result in superannuation benefits to the employees, since there are various conditions to be fulfilled by the employees like serving a stipulated number of years, reaching a

certain age etc. Further, the pension payments are subject to tax at the time of actual receipt by the employee after his retirement. This may lead to partial double taxation for the employee where the contributions had been taxed earlier also (when the contributions exceeded Rs. 1.5 lakhs).

Recommendation

- It is recommended that employer contribution to approved superannuation fund be made fully exempt from tax.

4.26.4. Taxation of Rent Free Accommodation (RFA)/Concessional RFA

Issues

- Section 17(2) of the Act provides for valuation of perquisite in case of provision of rent free accommodation by the employer to the employee or by way of concession in rent in respect of such accommodation provided. In case of accommodation provided by the employer other than Central Government or any State Government, Rule 3 of the Rules provides for valuation of perquisite at specified rate of 15% or 10% or 7.5% of salary based on the size of population as per 2001 census. However, the above method of determination of the perquisite suffers from various inequities**:-**
  - An employee staying in the same company owned accommodation will have a different perquisite value with increase in salary and further, employees with difference in salaries will have a different perquisite value in respect of the same accommodation.
  - The determination of the perquisite value of the accommodation based on the salary of the employee irrespective of the size/fair rental value of the accommodation is completely illogical and unfair.
  - The perquisite value in respect of accommodation provided to employees of Central/State Government is based on license fee charged for such accommodation as reduced by rent actually paid by the employee. The valuation rules cast discrimination between employee of Central/State Government and any other employee.

Recommendation

- FICCI recommends that the rule for computing perquisite value of rent free accommodation should be suitably amended. For computing the perquisite value, the value of the accommodation should be Fair Rental Value based on the valuation report obtained from the municipal authorities (without making any discrimination between employee of Central/State Government and any other employee).

4.26.5. Deduction for Investment in Infrastructure bonds

Issue

- Finance Act, 2010 had introduced section 80CCF w.e.f. April 1, 2011, which stipulated that deduction would be available to the individuals in respect of subscription in notified

long term infrastructure bonds. This deduction under section 80CCF of the Act was over and above the existing aggregate limit of deduction allowable under section 80C, 80CC and 80CCD of the Act. However, the said deduction was discontinued w.e.f. Assessment Year 2013-14.

Recommendation

- It is desirable that the benefit under this section is not limited for two years as the intent behind this introduction of this section is to promote raising of funds for infrastructural development.
- Accordingly, it is suggested that suitable changes be made in this section so that this deduction is available in future years.

4.26.6. Revival of Standard Deduction

Issues

- A standard deduction was earlier available to the salaried individuals from their taxable salary income. However, the same was abolished with effect from AY 2006-07.
- On the other hand, business expenses continued to remain as permissible deductions from taxable business income.
- It has to be appreciated that standard deduction is not a personal allowance and used to be given as a lump sum for meeting employment related expenses. In many countries like Malaysia, Indonesia, Germany, France, Japan, Thailand etc., allowance in the form of standard deduction is available for salaried employees for expenses connected with salary income.

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.
- 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.

4.26.7. Transportation Allowance - Section 10

Issues

- The transport allowance granted by the employer to the employee to meet his expenditure for the purpose of commuting between the place of his residence and the place of his duty is currently tax exempt up to Rs. 1600 per month in terms of Section 10(14) of the Act read with Rule 2BB of the Rules. The limit was marginally increased from Rs. 800 per month to Rs. 1600 per month in the last budget.

- The exemption limit of Rs. 1600 per month seems quite nominal considering the ever rising fuel costs and resultant conveyance costs.

Recommendation

- The exemption limit of Rs. 1600 per month needs to be considerably raised upwards, say to minimum of Rs. 3,000 per month to bring it in line with the rising conveyance costs.

4.26.8. Education Allowance and Hostel Allowance

Issues

- The education allowance granted by the employer to the employee to meet the cost of education expenditure up to two children is currently tax exempt up to Rs. 100 per month per child in terms of Section 10(14) of the Act read with Rule 2BB of the Rules.
- This exemption limit was fixed in the year 2000 with retrospective effect from 1 August 1997 and seems extremely minimal considering the burgeoning cost of education.
- The hostel allowance granted by the employer to an employee to meet the hostel expenditure on his child is currently exempt upto Rs. 300 per month per child upto a maximum of two children. This exemption limit was fixed in the year 2000 with retrospective effect from 1 August 1997 and is very minimal considering the cost of inflation.

Recommendation

- The exemption limit of Rs. 100 per month needs to be considerably raised upwards, at the very least to Rs. 2,500 per month to bring it in line with the rising inflation and cost of education.
- The exemption limit of Rs. 300 per month of the hostel allowance should be raised upwards to at least Rs. 5000 per month.

4.26.9. Reimbursement of Medical Expenditure

Issues

- Any sum paid by the employer in respect of any expenditure incurred by the employee on the medical treatment of self/ family is currently exempt from tax, to the extent of Rs. 15,000 per annum.
- This limit was last revised long back and needs to be revisited in light of the rising medical and hospitalization costs especially for private hospitals. Personal health has gained utmost importance for an individual. Medical expenditure plays a crucial role while planning the household budget.
- The expenditure incurred by/ for retired employees in respect of medical treatment on self/ family is currently not exempt from tax.

Recommendations

- The exemption limit was last revised from Rs. 10,000 to Rs. 15,000 by the Finance Act 1998. The current tax exemption limit of Rs. 15,000 per annum needs to be increased to at least Rs. 50,000 per annum.
- Further, the exemption in respect of expenditure on medical reimbursements/ hospitalization expenditure in approved hospitals should also be extended to retired employees.

4.26.10. Tax Exemption in respect of Leave Travel Concession (LTC) - Section 10

Issues

- Presently, the economy class air fare for going to anywhere in India is tax exempt (twice in block of four years). However, this exemption is being allowed only for travel within India.
- Lately, owing to low airfares and package tours, a number of Indians prefer going abroad, instead of availing LTC, particularly to neighbouring countries like Thailand, Malaysia, Sri Lanka, Mauritius, etc., as the fares thereto are at times less than for travelling to some far away destination within India.

Recommendations

- It is therefore recommended to grant tax exemption for economy class airfare for travel abroad also, so long these are within the overall airfare tax exemption conditions for travelling in India. Further, considering the current prevailing trend in respect of foreign travel, there is a need to include overseas travel as well for the purpose of exemption or at least to exempt proportionate expenses pertaining to travel within India in case of joint travel (within India and overseas destination).
- Further, under Rule 2B of the Rules, the amount exempt in respect of LTC by air is to the extent of the economy fare of National Carrier i.e. Indian Airlines. It is suggested that word “National Carrier” should be deleted from Rule 2B.
- Moreover, as per the current provisions, Leave Travel Concession/ Assistance is eligible for tax relief for 2 calendar years in a block of 4 calendar years. It is suggested that the concept of calendar year should be replaced with FY (April – March) in line with the other provisions of the Income Tax Law and further exemption should be made available in respect of at least one journey in each FY.

4.26.11. Taxation of Social Security Contributions in the hands of Expatriates - Section 17

Issues

- In respect of an expatriate employee deputed to India, the home employer and employee may be required to contribute to social security schemes under the local law of country. In most cases, the contributions made to these schemes may not vest on the employee at the time of making the contributions and thereby do not provide any immediate benefit to the employee. Further, the employee contributions may also be

mandatory under the law of the home country. Both the employer and employee contributions may be available as a deduction from taxable income in the home country of the expatriates.

- However, currently there is no provision under the Act, which provides for the taxability or otherwise in respect of such contributions from taxable income, though there have been several favourable judicial precedents to this effect such as CIT v. L.W. Russel [1964] 53 ITR 91 (SC), Gallotti Raoul v. ACIT [1997] 61 ITD 453 (Mum), ITO v. Lukas Floe (Pune) (2009-TIOL-556), CIT v. NHK Japan Broadcasting Corporation [Civil Appeal No. 1712 of 2009 – SC].
- Recently, even the Delhi HC pronounced the decision in case of Yoshio Kubo, wherein it was held that employer's contribution to overseas social security, pension and medical/ health insurance do not qualify as perquisite under Section 17(1)(v) of the Act and are not taxable in the hands of the employees.

Recommendation

- It needs to be clarified under the Act, that employer contributions to such social security schemes should be exempt in the hands of the individual employee based on the principle of vesting. Further, the employee contributions should be available as a deduction where the same are mandatory and constitute diversion of income by overriding title.

4.26.12. 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 expatriates may complete their assignments and leave India prior to obtaining their tax refunds which also creates issues with respect to credit of their refund amounts.

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.

4.26.13. 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.
- Term deposits for a period of 5 years or more with a scheduled bank, in accordance with a scheme framed and notified by the Central Government, by an individual/ HUF is eligible for inclusion in gross qualifying amount for the purpose of deduction under Section 80C of the Act. For other eligible investments such as bonds and mutual funds, the lock in period is 3 years and to ensure parity, the period of term deposits for claiming deduction under Section 80C of the Act should also be reduced to 3 years from existing 5 years.

4.26.14. Deduction under section 80C in respect of repayment of a loan from a foreign bank

Issue

Section 80C(xviii) of the Act allows deduction in of repayment of amount borrowed from specified lenders or categories of institutions such as public companies formed and registered in India, companies in which the public are substantially interested, etc. In case of ordinary residents whose global income includes income from house property outside India, they are not entitled to deduction as the lender would not fit into any of the specified categories. While the income earned from the property outside India is brought to tax by virtue of residential status, relief for repayment of borrowed amounts is not available under section 80C of the Act. This results in disparity between incomes from properties in India and those outside India. In respect of overseas house property, various deductions allowed

in the overseas countries such as depreciation, are not allowed in India, which leaves the individuals with very little tax credit that can be claimed in respect of overseas house property income. By not allowing the principal repayment on foreign loan as a deduction, the tax burden is significantly increased.

Recommendation

It is suggested that the provisions of section 80C of the Act be amended to include repayment towards a loan borrowed by the assessee from a foreign lender in case the income from property held outside India is taxable in India.

4.26.15. Overall deduction in respect of amount paid under Pension/Annuity Plans

Issue

- As per Section 80CCE of the Act, the overall ceiling for deduction is Rs.1.5 Lakhs for the payments covered by Section 80C, payment towards annuity plans covered by Section 80CCC and payment towards NPS covered by Section 80CCD.

Recommendation

- The overall ceiling limit of Section 80CCE should be enhanced to at least Rs. 3 lakhs to augment savings in the economy to promote economic growth.

4.26.16. Deduction for Educational Expenses

Issue

- Education of children these days imposes a heavy burden on the middle class. A good beginning was made in 2003 by providing deduction for tuition fees under Section 80C of the Act. But Section 80C of the Act is particularly a provision granting incentive for savings and also considering the long list of eligible investments in this Section, there is very little relief to the individual on account of the education fees incurred by him.

Recommendation

- It is therefore recommended to de-link deduction for educational expenses for children from Section 80C and provide under a separate provision like Section 80D of the Act for medical insurance. A reference to the Ministry of Education to find out the tuition fee for an average middle class household will give an indication about the limit of the deduction.

4.26.17. Deduction in respect of Rent paid by Taxpayers not receiving a HRA

Issue

- Under Section 80GG of the Act, the maximum deduction available to individuals who do not receive a House Rent Allowance (HRA), in respect of rent paid has been enhanced to Rs. 5,000 per month by the Finance Act, 2016 from the earlier limit of Rs. 2000 per month. However, the exemption limit to the extent of Rs. 5000 per month is very less compared to the inflationary effect on rent over the years.

Recommendation

- The exemption needs to be increased to at least Rs. 15,000 per month in view of the huge rental escalation. As in the case of HRA exemption, the Government may also consider introducing separate limits for metro and non-metro cities.

4.26.18. Deduction in respect of Interest on Deposits in Savings Account - Section 80TTA

Issue

- Section 80TTA was inserted by the Finance Act, 2012 to provide deduction of up to Rs.10,000/- in the hands of individuals and HUFs in respect of interest on savings account with banks, post offices and co-operative societies carrying on business of banking. However, it is unlikely that individuals would keep their entire savings in a savings bank account, which earns a much lower rate of interest as compared to term deposits. They are likely to transfer some portion of their savings to several deposits to earn comparatively better returns.

Recommendation

- It is suggested that the scope of Section 80TTA of the Act should be widened to incorporate all types of deposits (such as term deposits, recurring deposits etc.) made within the banking channels, thereby inducing savings for the growth of the economy. Further, the limit of deduction under this section may be increased from Rs. 10,000 to Rs. 20,000.

4.26.19. Electronic Meal Card

Issues and Recommendations

- In 2001, taxation of subsidized/ free meals as perquisite was introduced vide Finance Act 2001. The perquisite rules provided that any expenditure incurred by the employer on providing free/ subsidized meals to its employees during working hours beyond Rs. 50 per meal per employee was taxable in the hands of the employees. It is important to note that no change has been made in the prescribed exemption limit till date. In the year 2001, when the current limit of Rs 50 per meal for exemption purposes was first legislated, an employer could easily provide a sumptuous meal to his employees within the limit of Rs. 50 without having to levy any tax on the employees. The average cost of a meal at various outlets in 2017 which ranges between Rs. 225 to Rs. 375 per meal clearly highlights the insufficiency of the present limit of Rs. 50 per meal. It is recommended that tax-exemption limit of Rs. 50 per meal should be revised to at least Rs. 200 per meal, to factor in rising inflation and to keep the meal benefit meaningful and relevant for the employee.
- Many employers these days provide this facility through electronic meal swipe cards/digital vouchers. However, the current rules expressly provide exemption to paid vouchers and not electronic cards though such cards were expressly exempted under the erstwhile FBT regime subject to conditions. It is submitted that there are no policy considerations that justify making a distinction between electronic vouchers/ cards and paper vouchers. Electronic vouchers/cards are identical in all relevant aspects to paper

vouchers and hence, any distinction between the two for the purposes of the perquisite valuation rules is not warranted. Accordingly, it may expressly be clarified that the words "paid vouchers" used in the proviso to Rule 3(7)(iii) includes paper as well as electronic vouchers (i.e. electronic cards). It is accordingly recommended that the said exemption along with increased limit should be extended to electronic meal vouchers/cards.

- The prices of food products have been fluctuating significantly over past years and it is inevitable that the prices will keep on fluctuating in future as well. It is pertinent to note that the Act has already recognized the concept of indexation to adjust for inflation for the purpose of computing tax on long term capital assets. Considering the intent of the legislature to allow the benefits to the employees for availing facility of a sumptuous meal, it is recommended that the amount of exemption limit be linked with the Consumer Price Index (Food).

4.26.20. Exemption for payment of Leave Encashment - Section 10

Issue

- The exemption limit for leave encashment paid at the time of retirement or otherwise is notified by the CBDT in accordance with the powers given under Section 10(10AA) of the Act. The current limit of Rs. 3 lakhs was notified in 1998 and needs to be raised substantially with immediate effect.

Recommendation

- It is, therefore, suggested that the limit should be raised to Rs.10 lakhs in line with the increase in the limit of gratuity.

4.26.21. Income of Minors - to increase Exemption Limits under Section 10(32) of the Act

Issue

- As per Section 10(32) of the Act, in case the income of an individual includes the income of his minor child in terms of Section 64(1A), such individual shall be entitled to exemption of Rs.1,500 in respect of each minor child if the income of such minor as includible under Section 64(1A) exceeds that amount.
- The current limit of Rs. 1,500 was fixed by the Finance Act, 1992 and needs to be raised substantially with immediate effect.

Recommendation

- It is suggested that the limit of exemption under Section 10(32) of the Act should be raised to at least Rs. 10,000 for each minor child.

4.27. Other Direct Tax provisions

4.27.1. 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.

4.27.2. 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 as maximum tax saving for investor would be reduced by approximately Rs.60,000 (ie.30% of Rs.200,000) depending on tax slabs.
- 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.

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.

4.27.3. Set Off of brought forward Speculative losses

The Finance Act 2014 amended the Explanation to Section 73 of Act w.e.f 1st April 2015 (i.e. AY 2015-16) to provide that losses of companies having principal business of trading in shares will be treated as non-speculative. Further, clause (e) has been inserted to section 43(5) of the Act w.e.f 1st April 2014 (i.e. AY 2014-15), to provide that a transaction in respect of trading in commodity derivatives carried out on a recognized association to be non-speculative.

Whilst the above amendments have been done, the Act does not prescribe any mechanism for enabling set-off of earlier brought forward speculative losses from the same business or from trading in commodity derivatives.

Both the above amendments are hindering the ability of tax payers to set-off speculative losses incurred under the erstwhile provisions of the law against the income of the same business which is now treated as non-speculative due to the amendments.

Recommendation

It is recommended that it may be clarified that brought forward speculative losses on account of the above two reasons be treated as non-speculative for set-off in the current and subsequent years.

4.27.4. Deduction under section 80G

Issue

Deduction under section 80G of the Act is allowed in respect of donations to certain funds, charitable institutions etc., however, the deduction is restricted to the extent of 10% of gross total income. Even though there are many magnanimous donors who are willing to contribute funds to charitable institutions after ensuring that their donations are properly utilised, the overall ceiling of 10% of gross total income under section 80G of the Act impedes their way to contribute liberally and encourage more and more institutions.

Recommendation

- The ceiling of 10% on gross total income may be removed.
- Donations to Chief Minister's Relief Fund be allowed 100% exemption and accordingly suitable amendment be made in the provisions of section 80G of the Act.

4.27.5. Increase in de-minims limit for payment of advance tax

Issue

- The de-minimis limit of Rs. 10,000 for payment of advance tax has been last amended by Finance Act, 2009. In view of the above and considering the inflation in the economy it is proposed to increase the de-minimis limit for payment of advance tax.

Recommendation

- Current threshold of payment of advance tax where the tax payable is in excess of Rs. 10,000 should be increased to Rs. 1,00,000.

4.27.6. Timeline for filing a revised tax return

Issues

- The Finance Act 2017 has reduced the time limit to file a revised return from two years from end of the financial year to one year from the end of financial year. The amendment will apply in relation to AY 2018-2019 and subsequent years.
- This impacts many tax payers who have moved abroad for employment and qualify as Resident and Ordinary Resident (ROR) of India in the financial year of departure from India or any other ROR tax payer who has overseas income.

- This is on account of the fact that the relief to be claimed (if any) on any overseas income offered to tax could depend on the tax return to be filed in the host country/ country of source of income. It is possible that the tax return filing deadline in such country may be later than the timeline for filing the revised tax return in India. e.g. Mr. A moving to USA on 1 Jan 2018 and qualifying as a ROR of India for FY 17-18. His Jan 18-March 18 US income will be taxable in India subject to relief under the Indo-USA Double Tax Avoidance Agreement (DTAA). However, this relief can be determined based on his US returns for calendar year 2017 as well as 2018 and the deadline to file the US tax return for calendar year 2018 is 15 April 2018 (and further extendable as per US domestic tax law).

Recommendation

- Considering the hardship that can be caused on this account it is suggested that the timeline for filing a revised return should be restored to two years from end of the relevant financial year.

4.27.7. Investment Allowance - Section 32AC

The Finance Act (No. 2), 2014 has amended Section 32AC of the Act, wherein the taxpayer shall be allowed a deduction of 15% of cost of new plant and machinery, for investment made up to 31 March 2017, if such investments are more than Rs. 25 crore in a FY. Further, the taxpayer eligible to claim deduction under the earlier combined threshold limit of Rs.100 crore for investment made in FYs 2013-14 and 2014-15 shall continue to be eligible to claim deduction even if its investment in the year 2014-15 is below the new threshold limit.

The sunset date for investment allowance is March 31, 2017. To accelerate the growth of investments in the economy, it is submitted that the sunset date for deduction under section 32AC of the Act be extended from March 31, 2017 to March 31, 2020. It is further submitted that the allowance under Section 32AC of the Act should also be extended to other sectors of the economy like those in operating developing and building an infrastructure facility, telecom infrastructure service providers, processing/assembling activities, creation of broadband facility, and conversion of LNG into RLNG etc. This will truly provide a fillip to the economy and will meet the true intent of the provisions. Specific amendment to extend benefit of the investment allowance to service companies as well as infrastructure companies be made.

It is further recommended that the investment limit for MSMEs should be reduced suitably to enable them to take the benefit under section 32AC of the Act or a specific provision be introduced in the Act for MSMEs.

4.27.8. Calculation of Interest for delay in Deposit of Taxes deducted - meaning of 'Month'

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.

4.27.9. Interest Payable in case of Default in furnishing Return - Section 234A

Issue

- Where return of income is filed after the due date, interest under Section 234A of the Act is levied from the due date of filing return till the date of actual filing. Currently, while computing the amount on which interest is payable, self-assessment tax paid by the taxpayer is not considered. Consequently, the taxpayer has to pay a higher amount of interest.

Recommendation

- Since interest is not a penalty and the reason for levy of interest is only to compensate the revenue, in order to avoid it from being deprived of the payment of tax on the due date, it is suggested that in cases where the tax on self-assessment is paid under Section 140A of the Act before the due date for filing return on income but return has been filed after the due date, such tax on self-assessment should be considered as item of deduction for the levy of interest under Section 234A of the Act.

4.27.10. Modification of Income Tax Form to allow proper Disclosure

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.

4.27.11. 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.

4.27.12. Time Limit for completion of Appeals by Appellate Authorities

Issue

- The Act does not specify any time limit within which the appeals filed before the appellate authorities must be disposed of. This results in undue hardship and never ending litigation cost to the taxpayer.

Recommendation

- It is suggested that suitable provision may be incorporated in the Act to prescribe specified time limits for disposal of appeals in a timely manner at all appellate levels.

4.27.13. 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.

4.27.14. 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.

4.27.15. Relief from interest under section 234B

Issue

Section 234B of the Act provides for levy of interest for default in payment of advance tax. The interest liability is computed on the basis of delay in payment of installments prescribed. The newly incorporated entity should not be obligated to pay advance tax for the installments due prior to the date of incorporation. However, it has been observed that in practice, interest is levied by the income tax department.

Recommendation

It is suggested that interest under section 234B of the Act should be levied only for remaining installments after the date of incorporation. Appropriate amendment in this regard be carried out.

4.27.16. Non-levy of interest under section 234C in case of capital gains for MAT

Issue

Section 234C of the Act provides for payment of interest by assessee in case of shortfall between tax payable on returned income and advance tax paid (paid on estimated income) in specified quarterly installment. However, no interest is payable where there is failure on the part of the assesse to estimate or under estimate the capital gains and tax thereon is paid by March 31 of the financial year. It is to be noted that said exemption from payment of interest under section 234C of the Act in case of capital gains is applicable only for income computed under the normal provisions of the Act. No such benefit is available where capital gains form part of book profit for the purpose of computation of MAT. Thus there is an excess levy of interest under section 234C of the Act on capital gains under MAT.

Recommendation

It is suggested that the benefit of the exemption from payment of interest on capital gains (where tax thereon is duly paid by March 31 of the financial year) be also extended to capital gains included in book profit for MAT purposes through suitable amendment in section 234C of the Act.

4.27.17. Clarity on 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.

4.27.18. Search and seizure provisions

The Finance Act, 2017 has introduced a series of amendments in the Act expanding the enforcement powers of the tax authorities. The most noteworthy of these are the amendments to sections 132 and 132A of the Act which govern search and seizure operations.

"Reasons to believe" to conduct a search, etc.

It has been stated in the Memorandum explaining the provisions of the Finance Bill, 2017 that on account of some ambiguity created by certain judicial pronouncements in respect of disclosure of 'reason to believe', the Finance Act has amended the provisions of section 132 and section 132A of the Act to provide that 'reason to believe' or 'reason to suspect' shall not be disclosed to any person or any authority or the Appellate Tribunal.

While the amendments are made with a noble intent - to crack the whip on tax-evaders who take shelter under technical anomalies in the law and get away without paying any taxes, the same also confers unbridled powers to officials, and have seemingly tipped the scales in favour of the law enforcement agencies. Such unfettered powers without fastening accountability has raised concerns in business and investor community. It is humbly submitted that the Government must now ensure that such sweeping powers are tempered with more judicious use of search and seizure operations, coupled with checks and balances such that the rights of the taxpayer are protected.

Given the above, we respectfully submit the following recommendations on this issue:-

- The "reasons to believe" must be compulsorily recorded in writing and the same should be approved by the Commissioner, Principal Commissioner and the Directorate General of Income-tax (Investigation) before conducting a search operation. Each of the approving authorities must record their satisfaction independently based on the available information.
- The recorded reasons must also give a detailed description of the information in possession, the time when such information was found along with detailed reasoning as to why it is believed that the subject matter forms part or will form part of unaccounted income of the taxpayer.
- The reasons should be disclosed by the tax authorities during the course of assessment/ appellate proceedings. The same may also be admitted as "additional evidences" during the appellate proceedings. Non-disclosure of reasons would severely hamper the

fundamental rights of the taxpayer as he would have no wherewithal to challenge the underlying basis; thus, grossly violating the principles of natural justice.

- As stated by the Finance Minister during the Parliamentary debate, it should be clarified that such reasons can be placed before the Courts in the event of a challenge to formation of belief; in which event the Court would be entitled to examine the relevance of the reasons for the formation of belief.
- Taxpayers' concerns should be addressed through effective implementation of the new provisions and ensuring that the provisions are not misused. An orderly system to ensure that the officers do not act on whim, unsubstantiated suspicion or rumours needs to be put into place. Measures such as implementation of a strict internal code for granting authorisation for search, administering a strict audit mechanism, releasing timely instructions, updating of search manuals, guidance on code of conduct for search officials, etc. can go a long way in providing a non-adversarial tax regime to the taxpayers.
- On many occasions, it is found that the tax authorities extend the inquiry post-search operations to legal issues which are unconnected and are already settled in earlier years either in assessment or appellate proceedings. The tax authorities should not extend the course of their search and seizure operation to issues which are unrelated/ unconnected other than those forming part of recorded reasons.
- In order to ensure that the tax officials exercise their powers judiciously, provisions which enable fixation of accountability on tax officials / informants in cases where an assessee is acquitted by the High Court / Supreme Court must be introduced. In this regard, a reference may be drawn from parallel statutes (example, Section 22 of Central Excise Act, 1944 and Section 136 of the Customs Act, 1962) which fixes accountability on the tax officials in cases of vexatious search and seizure operations. Similar provisions in the Income-tax Act, 1961 will help in preventing misuse and overreach.

"Provisional attachment" of property

It has been stated that to protect the interest of revenue and safeguard recovery in search cases, the tax officers will now have the power to attach provisionally any property belonging to the assessee. This is in addition to vast powers which the tax officers already have under the existing provisions of the Act. (say, section 281B of the Act which also provides for attachment of property)

Any seizure/ attachment of assets is extremely disruptive for a taxpayer and hence such power must be exercised extremely judiciously. In addition to the guidelines/ safeguards mentioned in The Second Schedule, the following guiding principles should be adhered to before attachment of any property:

- Any provisional attachment of property of the taxpayer must be approved by a Panel of 3 members; say the Principal Director General, the Directorate General of Income-tax (Investigation) as well as by an independent member (say, a retired judge of High Court or Supreme Court).

- A show-cause notice must be issued to the taxpayer so as to provide him an opportunity to defend his case as to why a particular property should not be provisionally attached.
- Pursuant to explanation provided by the taxpayer in response to the show-cause notice, the tax authorities must pass a speaking order if it intends to proceed with the provisional attachment. Also, such order must be made appealable.
- The value of attached properties should not exceed the amount of tax which the taxpayer has supposedly evaded.
- Section 281 of the Act already grants sufficient powers to the tax authorities wherein certain transfers are regarded as void if made during the pendency of any proceeding under the Act. Thus, the provisions pertaining to attachment of properties during the course of search operations must be exercised only in rare circumstances where the tax authorities have reason to believe that the taxpayer will transfer/ sell the assets.
- The attached property should be released if the taxpayer makes satisfactory arrangements for payment of applicable taxes and interest.
- Also, relevant provisions should be introduced so as to ensure that such powers are not indiscriminately used.
- The third report of the Tax Administration Reform Commission (TARC) has also suggested that search and seizure operations should be limited to cases where hardcore tax evasion is suspected. To ensure this, economic intelligence should be better developed and exchanged. Non-invasive surveys based on credible information and a technology-based tax collection system, which is non-intrusive, should be used to identify non-filers.

4.27.19. Re-introduction of rebate in respect of STT and CTT

Issue and Recommendation

The deduction under section 88E of the Act of the Securities transaction tax paid was allowed as rebate from tax till AY 2008-09. However, the deduction was withdrawn w.e.f AY 2009-10 resulting into double taxation. It is suggested that benefit of section 88E of the Act be re-introduced in both the securities and commodities market, so that STT and Commodities transaction tax is allowed as a rebate against tax instead of being allowed as an expense for computing taxable income.

Options are going to be a new derivative instrument in India's commodity market. For making these products useful for hedgers and to encourage their use, STT should be exempted on Options on exercise. This exemption is also necessary because commodity Options would converge into respective underlying futures contracts upon which CTT would anyways be applicable. Thus, levying a transaction tax on Options on exercise would tantamount to double taxation. The structure of commodity Options with futures as the underlying, as permitted by SEBI, makes it different from the structure of equity Options, whose underlying lies in the cash market. Thus, the tax treatment on these markets would also have to be different keeping in mind their structural differences. Besides, Options

products in other market segments either are exempt from STT. It is therefore suggested that commodity Options should, therefore, at least be exempted from STT on exercise.

4.27.20. 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 tax payers.

4.27.21. Prosecution proceedings – Failure to pay TDS

Issue

Section 276B of the Act lays down the prosecution provisions for failure to deposit TDS. It has been observed that there have been cases selected for prosecution under the said provision by the income tax department, even in cases where the delay may not have been for significant period (say less than a month or two) and interest under section 201(1A) of the Act has been duly paid.

Recommendation

It is suggested that prosecution proceedings should be avoided in genuine cases. It is further suggested that parameters for identifying genuine cases of delay should be introduced.

4.27.22. Rate of Interest on Tax Refunds – 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.

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.

4.27.23. Penalty for under Reporting and Misreporting of Income – Section 270A

The Finance Act, 2016 has amended the provisions for levy of penalty on account of concealment of particulars of income or furnishing inaccurate particulars of income by inserting section 270A in the Act to reduce the discretionary power given to the tax officer and to bring objectivity, certainty and clarity in levy of penalty. It is provided in section 270A of the Act that the penalty at the rate of 50% of tax be leviable in case of underreporting of income and 200% in tax in case of misreporting.

Issues

- The way the provisions for levy of penalty under section 270A of the Act are worded, it is comprehended that any claim made by the assesse not accepted by the assessing officer for example disallowance of expenditure on account of difference in interpretation on a matter of a question of law would attract automatic penalty @50% of tax on under-reported income. This would entail unwarranted litigation. One instance of under-reporting is mere excess of income assessed over income returned, for which a 50% penalty is applicable. This implies that any disallowance made by the AO will be a case for levy of penalty, regardless of whether the disallowance is on account of a false or genuine claim, capable of different interpretations. It also creates a perception of the effective tax rate being much higher.
- There is no clear-cut explanation/definition of what constitutes misrepresentation or suppression. Further, no obligation has been cast upon AOs to prove the mala fide intention of assessees, though they have the power to levy the penalty.

Recommendations

- It is recommended that further necessary changes be made/guidelines released to ensure that the new penalty provisions are not arbitrarily applied by the tax authorities. Certain controls may be required in the effective implementation of the section. In order to reduce the practice of Assessing Officers treating every addition to the income as misreported as well as the fact that the new section does not require recording of satisfaction before imposition of penalty proceedings (as was required under the erstwhile section 271), it is desirable that a suitable control mechanism may be put in place. Accordingly, the provisions of section 270A of the Act need to be suitably modified to restrict scope of under-reporting or misreporting to only mala fide cases and to ensure that genuine assessees are not harassed. At a minimum, the earlier provisions for levy of concealment penalty or furnishing inaccurate particulars can be retained. Also, the onus to prove mala fide intention should be on the assessing officer, before levying the penalty. Suitable amendments in the Act be made to give effect to the above.

4.27.24. Fee for Default in Furnishing Statements – Section 234E

Issue

The levy of mandatory fee under section 234E at Rs.200/- per day for default in furnishing of statements of TDS under section 200(3) and TCS under section 206C(3) has been a matter of

debate ever since it came to be introduced with effect from 1 July 2012. The constitutional validity of section 234E of the Act has been challenged in different High Courts through various writ petitions and the Courts have in turn granted a stay against collection of such fees. It is widely believed that this levy is harsh, keeping in view the fact that a person committing defaults of delayed deduction or payment of tax is already inflicted with non-deductible penal interest of 12% or 18% per annum. Moreover, in cases of grave default of non-furnishing of such Statements beyond one year, there is also a provision for levy of penalty of Rs.10,000 to Rs. 1,00,000.

Recommendation

It is recommended that the provisions of section 234E be dropped as there are sufficient compensatory and penal provisions under the law viz. section 201, 271C and 221 of the Act. Alternatively, fee under section 234E of the Act be reduced to Rs. 50 per day.

4.27.25. 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 proposed that the CPC takes remedial action in cases mentioned in the Justification section and does not treat the returns as defective.

4.27.26. 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 assesse".

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.

4.27.27. Allow assessing officer to appeal against the order of Dispute Resolution Panel

Issue

After the amendment made by the Finance Act, 2016, an assessing officer is not allowed to appeal against the order of DRP. The amendment was made by the Government by omission of section 253(2A) and section 253(3A) of the Act through Finance Act, 2016. The objective of the amendment as stated in the Memorandum Explaining the provisions of the Finance Bill, 2016 was to minimize litigation.

The DRP that was intended to be a quality assessment filter, has lost its effectiveness due to the amendment brought in 2016 by the Finance Act. The Revenue has now been barred from appealing against its directions. There is an apprehension that this will restrict the freedom of DRP in passing directions favourable to tax payers. For the last two years, when DRP directions were appealable even by the Revenue, a distinct fairness in its directions was evident. DRP directions, therefore, should again be rendered appealable by the Revenue.

Recommendation

It is recommended that the assessing officer should be allowed to appeal against the order of DRP. Suitable amendments in the Act be made accordingly.

4.27.28. Reasons for reopening to be sent along with notice for reopening of assessment

Issue

Section 147 of the Act empowers an AO to reopen an assessment if he has "reasons to believe" that income has escaped assessment. The said notice does not spell out the reasons in proper detail. The section does not have any procedural requirements, but a practice has developed and been laid down by the SC in GKN Drive Shafts' case, to be mandatorily followed while reopening assessment. Presently notice is issued under section 148 of the Act and later, the assessee has to request for the 'reasons for reopening' from the AO. Thereafter the Assessing officer provides the reasoning. At the time of issue of notice for re-opening assessment the reasons for reopening must be sent along with the notice. This will simplify the reassessment proceeding procedure.

Recommendation

It is suggested that suitable amendment be made in the Act to follow the procedure laid down in SC ruling referred above.

4.27.29. Revision of the order

Issue

The Finance Act, 2015 amended section 263 of the Act to provide that an order passed by the Assessing Officer shall be deemed to be erroneous insofar as it is prejudicial to the interests of the Revenue if, in the opinion of the Principal Commissioner or Commissioner the required conditions are fulfilled. These provisions give wide powers to Principal Commissioner. Similar changes have not been made in section 264 of the Act for orders which are prejudicial to assessee. Sections 263 and 264 of the Act were introduced with similar intent, i.e., to revise orders passed by lower authorities that are prejudicial to the interest of either the revenue or the assessee. Such amendment to section 263 alone makes the provisions biased in favour of the revenue.

Recommendation

It is recommended that the earlier provisions of section 263 of the Act be reinstated. Alternatively, section 264 of the Act should be amended suitably to bring it in lines with section 263 of the Act.

4.27.30. 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 Girishbhai Darji (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.

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.

4.27.31. 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.

4.27.32. Change in due dates for payment of advance tax

Issue

As per section 211 of the Act, companies have to pay 15% advance income tax on or before the 15th June each year. This causes unnecessary hardship, since it is extremely difficult to compute taxable income within 75 days from the commencement of the financial year – projections for depreciation (due to new acquisition or sell), TDS certificates that may be received, for example, cannot be ascertained accurately. Moreover, projections of profitability tend to vary from month-to-month.

Also, the requirement to pay 100% of the amount computed as income tax on or before 15th day of March each year results in curtailing cash inflows of companies.

Recommendation

The provision requiring payment of 15% as advance income tax on or before 15th June in each year be removed. The schedule for payment of advance tax should be fixed in such a way that not more than 75% is payable as advance income tax on or before the 31st March each year, and 100% by 15th June of next financial year.

This will enable assessee to pay tax more correctly. Revenue collection of government will not be affected, as government will receive last instalment of advance tax in June, instead of first instalment. It is suggested that suitable amendment be made in the Act in this regard.

The amended dates for advance tax payment is suggested as follows:-

- First instalment - 15 September – 25%
- Second instalment – 15 December – 30%
- Third instalment – 15 March – 30%
- Fourth instalment – 15 June of next financial year – Jan 15%

4.27.33. Monetary Limit for Audit of Accounts

Issue

Currently the limits for audit of accounts of taxpayers are as follows:-

Particulars	**Existing Limit (Rs. Lakhs)**
Sales turnover/ Gross receipts of business	**100**

Recommendation

Given the growth in volume of economic activity, the limits need to be revised as under:-

Particulars	**Proposed (Rs. Lakhs)**
Sales turnover/Gross receipts of business	**500**

5.1.1. Apportionment of credit and blocked credits

The basic objective of introduction of Goods and Services Tax (GST) is to remove cascading effect by facilitating seamless flow of credit of tax paid on supply of goods and services at every stage of the supply chain. The mechanism of allowing Input Tax Credit (ITC) across goods and services at every stage of supply is the backbone of the GST regime. However, provisions in the GST law restrict the allowability of input tax credit in certain situations. Accordingly, the adversity of undesirable cost cascading effect still remains and needs to be addressed particularly in the below mentioned cases:-

(a) The GST law denies availability of ITC in respect of goods or services which are used for effecting exempt supplies. In case of high sea sale only the buyer who files the Bill of Entry for home consumption is liable to pay IGST. However, given the wider definition of exempt supply, the person who is making such sale may not be entitled to input tax credit pertaining to goods and services used for making such sale. Accordingly, the common credit pertaining to such sale has to be reversed. There seems to be no justification in denying the ITC in the earlier leg of the transaction when the Government is able to collect GST from the last buyer in the chain. The cost of denial/reversal of input tax credit may result in making such sales unviable. It is suggested that high sea sale should be treated as 'zero rated supplies' under the GST law and a suitable amendment made be made accordingly.

(b) As per the provisions of the GST law, no input tax credit is available in respect of specified goods and services. For instance input tax credit on Motor vehicles such as cars and other conveyances used for business purposes (subject to certain exceptions) is not allowed under the GST regime. It is believed that denial of input tax credit on motor vehicles will lead to breaking of the credit chain and maintenance of unwarranted records. It is also pointed out that when tax was collected at first point for which credit is not available then subsequent levy of tax on sale of such vehicles results into double taxation. It is suggested that ITC should be allowed in respect of motor vehicles and other conveyances used in the course or furtherance of business. Alternatively, exemption from GST should be provided on further sale/supply of such motor vehicles. It should also be clarified that credit in respect of lease of motor vehicle and buses is allowed.

(c) No input tax credit is available in respect of goods lost, stolen, destroyed, written off or disposed of by way of gift or free samples. The goods distributed by way of gifts/free samples or writing off of stock etc. take place in a normal business scenario and expense on these account are inbuilt in the sale price, which is subject to GST. This is typically true in case of promotional materials. Identifying the amount for reversal of ITC pertaining to such goods would involve a lot of unwarranted paper work. Similarly, ITC in respect of lost, stolen or destroyed goods should be allowed subject to a permissible

limit. It is suggested that provisions in the GST laws be appropriately amended to provide for allowability of input tax credit on the aforesaid goods.

(d) It has been provided in the GST law that where the goods or services or both are used partly for effecting taxable supplies including zero rated supplies and partly for effecting exempt supplies, the amount of credit is to be restricted to the extent it is attributable to the taxable supplies including zero-rated supplies. In case of capital goods, the amount of common credit attributable towards exempted supplies along with interest will be added to the output tax liability of the person claiming the credit during the useful life of the capital goods. The mechanism of apportionment of credit built in the GST law is extremely onerous to follow. Further, under the erstwhile regime, as per CENVAT Credit Rules, if the capital goods are used partly for effecting taxable supplies and partly for effecting exempt supplies no reversal of ITC is required. It is therefore suggested that suitable amendment be made in the provisions of section 17 of the CGST Act, 2017 to provide that goods would exclude capital goods for the purpose of reversal of ITC. It is suggested that entire input tax credit on capital goods should be allowed unless it is exclusively used for exempted supply of goods or services.

5.1.2. Do away with the requirement of E-way Bill

The industry operating on PAN India basis is quite concerned about the parallel documentation in the form of E-way bill. The GST IT system has not yet stabilized and huge effort is devoted to GST compliance affecting adversely the other business operations of an entity. It is strongly believed that the present documentation under GST could be used to track supplies without additional documentation in the form of E-way bill.

It is suggested that the Government may observe the functioning of the controls and procedures as provided for under the GST law over a period of time and only if concerns of revenue leakage persists, the alternative of E-way bill should be examined. The present IT system under GST is under serious pressure particularly for huge quantum of documentation and various interfaces. It is believed that addition of E-way bill for supplies would add more documentation and complexities to the business process. The various concerns of the industry should be examined for example regarding enhancing the threshold for generation of e-way bills, requirement of e-way bill for intra-State movement etc. and appropriate decision should be taken to ensure that introduction of E-way bill does not add to the complexities of doing business.

5.1.3. Reverse Charge Mechanism - Purchases from Unregistered dealers

The provisions of section 9(4) of the Central Goods and Services Tax Act, 2017 (CGST Act, 2017) and section 5(4) of the Integrated Goods and Services Tax Act, 2017 (IGST Act, 2017) provide for payment of GST by the recipient of goods and services, being a registered person, on reverse charge basis on purchases from unregistered persons. Further, the Government vide Notification No. 8/2017, central tax (rate) dated June 28, 2017 has granted exemption from CGST in respect of such supplies of goods or services provided such supplies does not exceed Rs. 5000 in a day. Various difficulties were observed in complying with the aforesaid provision as in an industry, there are various types of small value supplies

received from various unregistered suppliers for example supply of stationery, books and periodicals, food items etc. The provision when implemented had cast an onerous task on the company to identify each and every line item of small purchases made, identify the tariff code, pay applicable taxes for each such purchase, claim credit based on conditions prescribed under the law, issuance of invoice for a huge number of small transactions etc. Considering the complexities involved in the implementation of the provision and to benefit small businesses and substantially reduce compliance costs the Government has suspended provisions of section 9(4) of the CGST Act, 2017 and 5(4) of the IGST Act, 2017 till March 31, 2018. The decision of the Government is welcome as the provision triggers only unwarranted compliance burden on the recipient. It is believed that the compliance with the aforesaid provision is an impediment to a simplified tax regime. It is emphasised that the provision should be altogether removed from the GST laws.

5.1.4. Place of supply of services by an Intermediary

As per sub-section (8) of section 13 of the IGST law, the place of supply of intermediary services shall be the location of supplier of service.

The said provision shall negatively impact the intermediary in India who arranges or facilitates the supply of service to the foreign principal. Such Indenting Agents provide valuable services to the country by virtue of their expertise in procurement from overseas market by acting as agent of overseas suppliers. They facilitate supply of quality raw material and other goods as required by Indian manufacturers/customers. The services are ultimately provided outside India to a foreign principal. However, as per the aforesaid provision the services provided by an intermediary to any person outside India shall not classify as export and the same shall be taxable in India. The levy of GST on such services shall negatively impact the said sector by making the services more expensive due to GST of 18% on such services. The Indenting Agents, who are working on a very thin commission margin have to absorb GST @ 18% making their business unviable. Also the service consideration charged by Indian Intermediary is included in principal supply of goods or services by foreign supplier on which applicable customs duty/GST shall be payable. Levy of GST on intermediary services would lead to double taxation for the foreign principal as in certain countries recipient of service is required to pay tax in their home county on reverse charge basis.

It is suggested that the place of supply of service provided by Intermediary should be considered as the location of recipient of service.

5.1.5. Transitional Provisions

(a) Input Tax Credit on Capital Goods received after the Appointed Date

Section 140(5) of CGST Act, 2017 provides for transitional credit with respect to stock in transit. In a situation where capital goods have been imported on payment of customs duty prior to June 30, 2017 but are received in the factory after the appointed day, the narrow meaning of section 140(5) of the CGST Act, 2017 does not allow such credit to the importers. Section 140(5) does not include Capital Goods in transit. In fact, there is no transitional provision to claim credit of capital goods in transit.

It is requested that a suitable amendment be made in the Act to provide that credit of duties paid on capital goods in transit will be allowed in addition to credits of duties paid on Inputs & Input Services, even if such goods are received after the appointed date.

The transitional provisions under section 140(5) of the CGST Act, 2017 does not provide for any mechanism to claim credit of tax in respect of input services received on or before the appointed date, however, the invoice was in transit as on appointed date and/or received/paid subsequent to the filing of service tax return cut-off date i.e. August 15, 2017. In such cases credit which would have otherwise been eligible under the erstwhile regime would be denied in absence of provisions to claim such credit under the GST regime. It is requested that appropriate amendment be made to allow credit for such input services under the GST regime.

(b) **Carry forward of Transitional Credit to Depot of a manufacturer and Work Contractors**

Section 140(3) of the CGST Act provides that a registered person, who was not liable to be registered under the existing law, or who was engaged in the manufacture of exempted goods or provision of exempted services, or who was providing works contract service and was availing of the benefit of notification No. 26/2012—Service Tax, dated the 20th June, 2012 or a first stage dealer or a second stage dealer or a registered importer or a depot of a manufacturer, shall be entitled to take, in his electronic credit ledger, credit of eligible duties in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the appointed day subject to the following conditions, namely:—

i. such inputs or goods are used or intended to be used for making taxable supplies under this Act;

ii. the said registered person is eligible for input tax credit on such inputs under this Act;

iii. the said registered person is in possession of invoice or other prescribed documents evidencing payment of duty under the existing law in respect of such inputs;

iv. such invoices or other prescribed documents were issued not earlier than twelve months immediately preceding the appointed day; and

v. the supplier of services is not eligible for any abatement under this Act.

From the above it is clear that a depot of a manufacturer can carry forward the taxes paid under the earlier law in respect of only those invoices which are pertaining to a period upto twelve months before the appointed date. If any goods have been procured more than twelve months before the appointed date and were lying in stock as on June 30, 2017 then the taxes paid under the earlier law will not be allowed to be carried forward. There seems to be no justification in not allowing credit in respect of invoices which are more than a year old as the supply of such goods and services made after the appointed date would be subject to GST. Under the erstwhile regime, there was no restriction of a period of one year to a manufacturer depot. It is suggested that necessary amendment in law be made to delete the restriction of any period for carry forward of taxes paid under the earlier law.

Secondly, the provision does not allow credit of tax in respect of input services contained in semi-finished or finished goods held in stock on the appointed date. The credit for such

input service (which was a cost in erstwhile regime) is not allowed to be carry forward as transitional credit. Appropriate amendment be made in the provision of section 140(3) of the CGST Act, 2017 to allow transitional credit in respect of input services contained in semi-finished or finished goods held in stock on the appointed date.

Further, section 140(3) of the CGST Act, 2017 specifically provides the benefit of ITC carry forward from the erstwhile regime to GST regime only to registered person who was providing works contract service and was availing of the benefit of Notification No. 26/2012—Service Tax dated the 20th June, 2012. In other words, works contractors not availing the benefit of 26/2012 and following Rule 2A of the Service Tax (Determination of Value) Rules 2006 are not having clarity as to if they are allowed to transition the ITC in-build in the materials lying in their stock with the tax invoice in the name of the stock point as well as goods transferred and received/held in stock under delivery challan but not under tax invoice (where tax invoice available in the name of distribution center of the same legal entity) as on the transition date.

The registration under the erstwhile service tax was only in relation to the service portion of the works contract and not in relation to goods portion of the works contract. Hence, clarity is expected as to if the excise duty and CVD paid on goods held in stock which would be incorporated in the works on execution of works contract, would be covered under section 140(3) of the CGST Act, 2017. Suitable clarification be provided in this regard at the earliest.

Further, appropriate procedure is also expected in this context for claiming transitional credit under Section 140(3) on the lines of Rule 117 of CGST rules.

(c) Carry forward of Krishi Kalyan Cess and Education Cess

In terms of section 140(1) of the CGST Act, 2017, CENVAT credit carried forwarded in the return filed under the existing law is permitted to be transitioned as CGST credit. In terms of Notification No. 28/2016 dated 26 May 2016, Krishi Kalyan Cess ('KKC') paid on services was available as CENVAT credit. Similarly, Education Cess ('EC') and Secondary and Higher Education Cess ('SHEC') paid in relation to goods and services was permissible as CENVAT credit. Thus, unutilized balances of KKC, EC and SHEC carried forward in the service tax returns under the existing law should be permitted to be transitioned as CGST credit. It is suggested that appropriate clarity be provided in this regard.

(d) Requirement for transition provision to take ITC for eligible credits under the existing law which are within the one year time period specified under the existing law

Under the CENVAT Credit Rules (referred as 'existing law' in GST Acts), assessee are eligible to take credit within one year from the invoice date. There are instances where various assessees have missed to take certain input credits in their last Excise or Service Tax or VAT returns example they come across such instances during closure of their audit/tax audits. Going by the provisions of existing law they were eligible to claim the same, had the existing law continued. Transition provisions provide solution only in respect of transfer of closing balances under the last return under the existing law, unavailed credit on capital goods and credit on in-transit goods/services. However, there is no provision to allow credit for genuine cases which got omitted to be taken in the last return under existing law. This leads

to undue tax burden to the industry. Suitable provisions may be added/amended and procedure be prescribed to enable taking of such missed credits.

(e) Transition credit for payments made due to Department Audit/Assessment findings

Post implementation of GST, during the department audit or assessment, assessees are required to make payment of taxes under reverse charge for any of the omissions earlier and the provisions of existing law allowed them to take credit for the same. However, under the current transition provisions, there is no possibility of taking this credit as the last date for filing return or revised return under the existing law has been over. Considering this, assessees are having the hardship of paying the taxes without any solution to take input tax credit or refund (in case of exporters). Considering this situation, suitable amendments be made in the GST law to provide for GST transition provision.

5.1.6. Provide exemption from registration

Section 24 of the CGST Act, 2017 specifies the requirement for compulsory registration for a non-resident taxable person. The section specifies certain categories of persons who are mandatorily required to register under the GST Act and are not governed by the minimum threshold limit of Rs. 20 lakh/10 lakh. Thus every non-resident individual or company will have to obtain a registration under the Goods and Services Tax who occasionally undertake transaction involving supply of goods or services or both, but who has no fixed place of business or residence in India.

Registration for non-resident will result into increase in compliance for technical individuals coming to India for providing the technical support to business in India. Under the erstwhile regime of service tax, there is no such requirement cast upon the non-resident coming to India and providing the technical support and the responsibility to pay tax was cast upon the service recipient.

Such additional burden for registration for non-residents under the GST regime who do not understand the law, language, culture prevailing in India and further payment of tax in advance will act as a big deterrent for foreign individuals coming to India and providing the technology support to Indian businesses. It is suggested that requirement for registration for non-resident under the GST regime shall be dispensed with for transaction covered under a contract with a registered person who should be made liable to pay tax under reverse charge.

As per the provisions of Section 24 of CGST Act, a person who is required to pay GST under reverse charge shall mandatorily take GST registration. Therefore, a person making exempt supply of goods or services or both is also liable to take registration under GST to make payment of GST under reverse charge. To reduce the unwarranted compliance burden, it is suggested that a person making supply of only exempted goods or services should not be made liable to take GST registration and make payment of GST under reverse charge mechanism.

Thirdly, the Government has exempted the registration requirement for service providers making inter-state supplies of services if their annual aggregate turnover is less than Rs. 20

lakhs (Rs. 10 lakhs in special category States except Jammu and Kashmir). To reduce the compliance cost of the small taxpayers, it is suggested that the exemption for registration be provided even to the supplier of goods making inter-state supplies of goods if his aggregate turnover is less than Rs. 20 lakhs (Rs. 10 lakhs in special category States except Jammu and Kashmir) in line with the exemption provided to the service providers.

Lastly, various companies in IT/ITES sectors are involved in providing services from client location such as maintenance service, BPO services, etc. The contract may require deployment of employees of IT/ITES companies at client location beyond a period of three months. This leads to practical difficulties in terms of obtaining registration at customer location i.e. submission of documents and also in terms of conduct of audit and assessment at the client location. It is suggested that such client location should not be considered as fixed establishment/location from where the services are provided upto certain threshold of value of business. In such cases, the location of project team/ base location of employee could be considered as the location from where the services are provided.

5.1.7. Credit of Coal Cess

Coal is a basic raw material and is extensively used in running the captive power plant of a manufacturing industry. Hence levy of coal cess @ 400 per ton under GST regime without input credit would inflate the cost of production and would increase the final rate of goods and services. The GST law was promoted as one nation one tax. However, the legacy issues like cess continue to find place in GST regime which was otherwise sought to have been subsumed in to GST.

The levy of cess should not in any way violate the principle of 'one nation one tax' as well as the principle of seamless input tax credit. It is accordingly suggested that coal cess should be done away with or credit for this cess be allowed against the output GST liability of the supplier.

Further, there is no clarity with respect to eligibility of credit of clean energy cess paid on purchase of coal in pre-GST regime wherein sale of coal is made in GST regime with applicable GST and compensation cess. It is suggested that appropriate clarity should be brought in to allow credit of clean energy cess paid on purchase of coal in pre- GST regime for set-off against the GST and compensation cess on payment in the post GST regime for stock as on transition date.

It is also pointed out that sale of even reject coal is subject to levy of GST of Rs. 400/MT, however, sale price of reject coal is lower than Rs. 400/MT. Reject Coal is mere wastage generated out of certain process and levy of compensation cess is making transaction commercially unviable. It is suggested that levy of compensation cess shall not be made applicable in case of sale of reject sale.

5.1.8. Place of supply of accommodation services

As per section 12(3)(b) of the IGST Act, 2017, the place of supply for services by way of lodging accommodation by a hotel, inn, guest house, home stay, club or campsite, by whatever name called, and including a house boat or any other vessel; or services by way of

accommodation in any immovable property for organizing any marriage or reception or matters related thereto, official, social, cultural, religious or business function including services provided in relation to such function at such property shall be the location at which the immovable property or boat or vessel, as the case may be is located. Therefore, the place of supply of accommodation services is the location of the immovable property and accordingly the supply is classified as intra-state supply leviable to CGST and SGST. Most corporates are not likely to be registered across all the states in India. Further, as per input tax credit utilization rules, the input tax credit of Centre and State tax cannot be cross utilized, thus the GST paid in the State becomes cost to the business and discourages businesses to go and held seminars, conferences in the other States.

It is suggested that place of supply of accommodation service provided to a registered person (Business to business) shall be the location of recipient of service instead of location of immovable property. Place of supply of accommodation services provided to an unregistered person shall be the location of immovable property as per the existing provisions. A suitable amendment be made in the law to give effect to the aforesaid suggestion. This will achieve the objective of extending seamless flow of credit and avoid any harm to the tourism industry.

5.1.9. Intra entity transfer of services

Collective performance of services by multiple branches/offices cannot be treated as supplies between branches inter-se. It will result in taxing artificial transactions and not economic transactions. It is requested that supply of service within the same legal entity from one vertical or division or office to another for use/consumption in the same legal entity should not be made liable to GST.

5.1.10. Input Service Distributor (ISD) should be allowed to discharge reverse charge obligation

Under the service Tax regime an ISD was allowed to discharge tax liability under reverse charge provision without seeking separate registration. However, under GST regime, an ISD is required to seek a separate GSTIN no. other than the ISD registration for discharging reverse charge tax liability. This is adding to the multiplicity of registrations and complexity in documentation and compliance. The requirement under the GST law for a separate registration by an ISD is only adding to complexity without any useful purpose being served. This is also an area impacting the matrix of 'ease of doing business'. It is suggested that GST law be amended to provide that ISD registration would serve dual purpose of distribution of central input tax credit and discharge of tax liability under reverse charge provision.

It has also been observed that cross charge mechanism method for distribution of credit does not require separate registration and is easier to implement. It is suggested that appropriate clarity be provided so that distribution of input tax credit by way of a cross charge invoice is allowed and the same is not disputed in future.

Rule 39(1) (a) of CGST Rules requires that input tax credit availed in a particular month should be distributed in the same month and the detail thereof shall be furnished in the FORM GSTR-6 in accordance with the provision of chapter VIII of the CGST Rules. The

provision will cause unnecessary hardship to a registered person in case he is unable to distribute the credit in the same month due to genuine reasons. It is recommended that input tax credit pertaining to a particular month should be allowed to be distributed any time before filing of annual return for the relevant financial year in which input tax credit was availed.

5.1.11. Levy of GST on services relating to exports of services relating to research and development, technical testing etc.

As per the provisions of the GST law, export of services such as research and development, technical testing and analysis, services relating to re-engineering which require the temporary import of equipment, vehicle on the article into India for carrying out clinical trials, technical testing or re-engineering processes have been subjected to levy of GST for the reason that the goods were worked upon in India without appreciating that the agency had exported the services in the form of results to the foreign parties for use outside India and consideration is received in convertible foreign exchange.

The levy of tax on export of such services even after re-exports of the article, vehicle or equipment after completion of the study is not justified and hampers the growth of such export industry in India. The additional tax liability on export of such services is adversely affecting the margins of the exporters who are already operating at thin margins and thus making the business in India unviable. It is suggested that necessary amendment be made in the GST law to provide that place of supply for services provided in respect of goods that are required to be made physically available by the recipient of service to the supplier of service shall be the location of the service recipient instead of the place where the services are actually performed.

5.1.12. Tax wrongfully collected and paid to the Central Government or State Government

As per the provision of section 77 of the CGST Act, 2017 and section 19 of the IGST Act, 2017, if a registered person has paid the CGST and SGST or CGST and UGST on a transaction considering it as 'intra-state' supply which was subsequently held to be an 'inter-state' supply would be allowed the refund of CGST and SGST paid by him. The registered person would however be required to pay the integrated tax due on such a transaction. Similar provisions for allowability of refund of IGST are there in case an 'inter-state' supply was subsequently held as 'intra-state supply'. It has been observed that this mechanism would result in payment of tax two times by the registered person. He would have to then claim refund by following the procedure contemplated under the law. This would lead to blockage of working capital for the taxpayer and further increases compliance cost for the taxpayer. It is suggested that a mechanism may be evolved whereby the taxpayer may not be required to pay tax twice in case the transaction is merely classified wrongly.

5.1.13. Clarification on GST on recovery of insurance premium or canteen expenses from the employees

It is a normal business practice for a company to enter in to an agreement with the Insurance Company to cover the life and health of its employees including their family. The insurance policy is in the name of the Company with the list of beneficiaries (i.e.

employees). As per the terms of employment contract, a part of insurance premium is borne by employer and the rest is recovered from the employee by debiting his salary. Similarly a company incur catering expenses to provide food to its employees and recover the same from employees.

The company discharges full GST on the insurance premium paid to the insurance company and on the catering expenses. However, there is no clarification as on date to provide that part of the recovery of premium and canteen expense made from the employee will not be subject to tax again in the hands of the company. A suitable clarification be issued in this regard to provide that recoveries towards insurance premium or canteen expenses from employees when the entire insurance premium or catering expenses has suffered GST on the full value of service shall not be subject to tax again in the hands of the company.

5.1.14. Issues related to Exports and Imports

(a) Details of multiple invoices against one shipping bill

As per the provisions of the GST law supply for export is zero rated provided certain conditions are fulfilled for example furnishing of information such as name and address along with country of the recipient on the invoices. In the case of large manufacturer exporter, a number of GST invoices are raised from the factory/mines based on which goods are first moved to the port which may be situated within the State or outside the State and after custom compliances goods are loaded in to the vessels for dispatch to other country. As per the format of Shipping Bill provided under the GST regime, details of all GST invoices are required to be mentioned in the shipping bill. Further, while filing GSTR-1, details of all GST invoices including the respective Shipping Bill no. is also required to be uploaded on the website of GSTN. However, at the time of filling Shipping Bill in the Customs EDI website, the option of mentioning multiple GST invoice details is not being provided in the case of export under Bond or letter of undertaking. The manufacturer exporters are apprehensive that since all the GST invoices are not being mentioned in shipping bill uploaded on the customs EDI website, a mismatch may happen between the GST invoices uploaded onto GSTN vis-à-vis EDI website. As a result of such mismatch, issue could arise in claiming export benefit by the exporters without any default on their part. It is suggested that format of shipping bill be amended or EDI website may be amended to provide for reporting multiple invoices against a shipping bill.

(b) Treatment of Iron Ore Export under GST

As per proviso to section 54(3) of CGST Act, 2017, no refund of unutilised input tax credit shall be allowed in cases where the goods exported out of India are subjected to export duty.

There is an apprehension specifically among the iron ore exporters that as a result of the aforesaid proviso an issue could arise in claiming refund of input credit lying in account by exporters of iron ore as iron ore below Fe 58% is subjected to export duty at Nil rate. It is submitted that the mining lessees as well as contractors providing support services to the mining industry are charging the applicable GST on supplies made to the exporter. It is requested that the above proviso be withdrawn as it defeats the very purpose of zero rating

of exports and would make the iron ore exporters uncompetitive in the international market.

(c) Furnishing of Letter of Undertaking in Case of Export of Services

Under section 16 of the IGST law, read with Rule 96A of CGST Rules, 2017

a) `a registered person is permitted to export in the following two ways:

- On payment of tax on the outward supply, with a subsequent claim of refund of the taxes paid
- Without payment of tax under bond or letter of undertaking ('LUT'), with a subsequent claim of refund of input tax credit

In the past, service exporters did not have to provide a letter of undertaking while exporting services without tax. This is therefore a new requirement that has been brought in for service providers, however, the requirement of having such a process for service providers is not clear. The process of filing letter of undertaking adds to the documentation burden and increases unwarranted compliance in the hands of the exporter. The exporter of services are placed at a disadvantage under the GST regime vis-à-vis the erstwhile which is against the intent of the Government. It is suggested that the condition of executing LUT be withdrawn in case of export of services.

(d) Mechanism to calculate IGST on import of goods

IGST is leviable on the value of imported goods and for calculating IGST on any imported article, the value of such imported goods would be the aggregate of:

i. the value of imported article determined under sub-section (1) of section 14 of the Customs Act, 1962 or the tariff value fixed under sub-section (2) of the that section; and
ii. any duty of Customs chargeable on that article under section 12 of the Customs Act, 1962 and any sum chargeable on that article under any law for the time being in force as an addition to, or as duty of Customs but does not include to the tax referred in the sub-section 7 (of the Integrated Goods and Services Act, 2017 (IGST Act) and sub-section 9 (The Goods and Services Tax (Compensation To States) Act, 2017).

Further, for Export Oriented Units (EOU), while the Basic Customs Duty (BCD) is exempted, IGST is required to be discharged on imports. The taxable value for the purpose of IGST on Imports is calculated as follows:

Assessable Value (AV) + BCD + Cess. [Since the BCD is exempt for EOU's, the IGST should then be calculated only on AV].

However, on the clearances of goods by EOU post GST, it is observed that the Customs EDI Software has been configured so as to compute IGST on [AV+ Notional BCD & Cess value], even in cases where BCD is exempt. Also, under the Customs Tariff Act, the computation of additional duty of customs (CVD) was similar to IGST Act. Hence, there should be no reason as to why the IGST is required to be paid on the deemed BCD & Cess value.

Accordingly, it is requested that appropriate clarification be issued prescribing methodology for computation of IGST on imports as per above discussion and necessary changes be made in the Electronic Data Interchange (EDI) portal so that tax is calculated on the appropriate value.

(e) Sale of goods on bond transfer basis

There is a business model whereby a dealer imports the goods into India in bulk and files in-bond bill of entry for clearance of same to bonded warehouse without payment of customs duty. Subsequently, the goods are sold in small quantities whereby the retail buyer files the bill of entry for home consumption and pays customs duty including IGST. In case of sale on bond transfer basis, sale happens after filing of bill of entry for warehousing but before filing bill of entry for home consumption. There are different interpretation issues leading to payment of GST twice, once at the time of import and once as chargeable by bulk dealer to retail buyer. In this regard, CBEC has issued a circular No. 46/2017-Customs dated 24/11/2017 which clarifies in case of sale on bond transfer basis, IGST would be leviable on sales made within bonded warehouse along with IGST that need to be charged at the time of filing of bill of entry. This has resulted in double taxation and huge working capital blockage for retail buyers, most of whom are exporters. Hence, it is suggested that sale on bond transfer basis should be considered as zero rated supply. In this manner, there would not arise issues regarding double taxation as well as any input tax credit reversal in the hands of retail buyer.

(f) Duty Credit Scrips under Exports

The exporters were getting duty credit scrips from Directorate General of Foreign Trade, which was utilized towards payment of import duty on import of raw materials. However, under the GST regime the scrip can be utilized only towards payment of basic custom duty and not IGST and compensation cess. As a result, IGST on imports has to be paid by the exporters in cash instead of adjustments through MEIS/SEIS license. This would result in additional working capital blockage for the exporters under the GST regime vis-à-vis the erstwhile regime. This denies the very basic purpose for which the scrips are granted. It is suggested that MEIS/SEIS license be allowed to be utilized towards payment of IGST on imports.

(g) Refund of Input GST (CGST/SGST/IGST) for Deemed Exports under Bond/Letter of Undertaking ('LUT')

Process for refund on GST on inputs paid on deemed exports by suppliers to holders of Advance Authorization/Export Promotion Capital Goods and 100% EOU is also pending for implementation. The input GST refund process for deemed export supplies should be notified and implemented at the earliest.

(h) On-line application and allotment facility for LUT/Bond Approval issuance (for export without payment of IGST)

The present system of granting LUT for Exports without payment of IGST involving physical submission of documents results in delays on account of diverse documentation

requirements suggested by the jurisdictional approving authorities. The online LUT application for exporters through GSTN portal login be notified and implemented.

(i) Clarity on the reduction in Duty credit scrips GST tax rate to zero percent

While the Government's notification for reducing the GST tax rate on duty scrips to 0% is welcomed by the industry, there is an ambiguity whether Supply of such Duty Scrips would be considered as 'Exempt Supply' and is required to be considered for the purpose of Input GST reversal. The issuance of the notification clarifying the position in the matter (i.e. whether input GST reversal required / not required) would provide certainty on this matter to the trade and industry.

(j) Details/Process of proposed E- Wallet facility for Exporters to be shared for trade/ industry feedback

The Government's proposal of E-Wallet facility for direct credit of advance refund into Exporters bank account should be put for public /industry feedback. The draft E-wallet facility proposal should be circulated for feedback by the trade and industry.

(k) Clarity on availability of refund of the opening CGST/SGST/IGST credit balance as on 1st July 2017 for Exporters

Clarity is required from the Government for allowance of opening input tax credit claim as a refund by Exporters/Merchant Exporters. It is requested that the position on claim of refund of opening balance by Exporters (whether can be claimed in the first refund application/can be claimed as unutilized at end of financial year) be clarified.

(l) Clarity on Refund of Input Tax Credit on Capital Goods used by Exporters

It is requested that clarity may be provided as to whether input refund can be claimed for GST paid on capital goods by exporters as only ' inputs/input services' have been specified under refund provisions. The availability of refund of GST paid on capital goods used for exports may be clarified.

5.1.15. Invoice, Debit and Credit Note Related Issues

(a) No penalty for Invoice series mismatch

As per the provisions of Rule 46 of CGST Rules, 2017, invoice should be consecutively and serially numbered uniquely for each financial year. Accordingly, an entity will have to maintain separate series of invoices for each GST registration i.e. state-wise. During the implementation of GST, a lot of assesses have faced serious hardship in configuring separate invoice series in their billing system and there could be lapses due to which they may be maintaining a single invoice series pan India across all GST registrations. Considering this is the initial phase of GST implementation, it is suggested no penal consequences due to non-maintenance of separate invoice series for each GST registration by a single entity be triggered.

(b) Issue of revised invoice and Credit note against each original invoice

Further, as per Rule 53 of CGST Rules, it is mandatory to give a serial number and date of the corresponding tax invoice on all the credit notes which are issued. It is practically not possible in multiple cases due to timing and stock holding situation to assign an original invoice link. Implementation of provision of the law in this form will lead to unwarranted compliance.

5.1.16. Basis for determining the number of Quarters for calculation of depreciation on repossessed assets

As per Rule 32(5) of CGST Rules, 2017, purchase price for the determination of value of supplies on sale of repossessed assets shall be deemed to be the purchase price of such goods by the defaulting borrower reduced by five percent for every quarter or part thereof between the date of purchase and the date of disposal by the person making such repossession. Further, as per section 2(92) of the CGST Act, quarter shall mean a period comprising three consecutive calendar months, ending on the last day of March, June, September and December of a calendar year.

From the perusal of the aforesaid, it has been observed that there could be an unwarranted situation in case the asset is used for say just 30 days, depreciation may be required to be calculated for 2 quarters. Some calculations of quarter is given below which does not seem to be in line with the intent of the Government.

Purchase Date	Sales Date	No. of Days	No. of Quarter (as per CGST Act)	No. of Quarters (on day basis)
A	B	C	D	E
29.06.2017	07.07.2017	8	2	0.08
02.06.2016	01.07.2017	394	6	4.38

It is therefore requested that a suitable amendment be made in the law to provide that the number of quarters be based on number of days on the basis of 90 days in one quarter with suitable provision for rounding off.

5.1.17. Restrictions on input tax credit

GST paid on supply of food and beverages, outdoor catering is restricted for input tax credit. However, in respect of rent-a-cab and employee related insurance, the law provides that the credit shall be allowed if it is obligatory for an employer to provide the same to its employees under any law in force. With these provisions, expenses incurred on food and beverage for any purpose will be disallowed including for the purpose of business conference, corporate events, seminars etc. Similarly, credit of works contract services when supplied for construction of immovable property (other than plant and machinery) is restricted except to a works contractor who is engaged in providing such services. Section 17(5)(d) of the CGST Act 2017 restricts credit in respect of goods or services received by a

taxable person for construction of an immovable property on his own account, other than plant and machinery, even when used in course or furtherance of business. There is no reason why credit on Motor vehicles used for business purposes, or credit of catering services or cab services is disallowed when such expenditure is incurred in the course or furtherance of business and even allowed under the Income Tax Act.

It has been further provided in the Explanation to section 17(5) of the CGST Act, 2017 that pipelines laid outside the factory premises are not 'plant and machinery'. In a large manufacturing company huge pipelines are commissioned for various purposes i.e. for taking water from river for being directly used in the manufacturing purpose. In such cases part of the entire pipeline system is inside the factory and part remain outside the factory. However it is a part of entire pipeline system which is used for furtherance of business only and accordingly suitable amendment should be made in the GST law to allow ITC on the entire pipeline.

Further, the restrictions regarding the availment of credit on goods lost, stolen, destroyed, written off or disposed of by way of gift or free samples has put questions on the normal business practices and the way in which the business is being carried. These restrictions on availment of ITC on genuine business expenditure have adversely affected the businesses to a large extent.

It is accordingly suggested that suitable amendments in the GST law be made to allow ITC on all expenses incurred for business purpose.

5.1.18. Audited Annual Accounts and reconciliation statement

Section 35(5) of the CGST Act, requires every registered person whose turnover during a financial year exceeds the prescribed limit to get its accounts audited by a chartered accountant or a cost accountant and submit a copy of the audited accounts along with reconciliation statement as mentioned under section 44(2) of CGST Act, 2017. However, the format for the audited accounts and audit report is yet to be prescribed. It may be noted that providing details for Non GST/exempted items of expense/income and assets/ liabilities which are not directly related to GST would be very difficult, as many of items would be incurred only at corporate level. e.g., borrowings and the related interest cost, employee cost, depreciation etc. Accordingly, the exempt/nil rated or Non-GST items may be excluded from the purview of audited accounts in respect of State offices.

5.1.19. Port Disbursement Charges

CIF contract comprises of cost of the imported material, insurance and ocean freight. In the case of CIF import, the obligation to arrange for transportation rests with the exporter who enters into a chartered party agreement with the shipping line for agreed amount of ocean freight. The service provider (the shipping line) and the service recipient (exporter) both are located in non-taxable territory. The ocean freight incurred in the transportation of goods imported into India is included in the value of goods and is subject to GST. Further, the same is also subject to GST as a supply of service on reverse charge basis by the importer. This leads to double taxation and therefore, it is recommended that ocean freight may be

exempted from levy of GST as a supply of service when the same is in relation to transportation of imported goods.

Further, ocean freight inter-alia includes the following charges called PDA Charges:-

- Pilotage & Towage
- Berth Hire
- Shifting & Anchorage fees
- Port Dues
- Cold Movement
- Fresh Water Supply

Out of the aforesaid, charges for pilotage & towage, berth hire, shifting and anchorage constitutes "Port Disbursement A/c Charges ('PDA')" and forms major component of ocean freight. Port issues a tax invoice for PDA charges in the form of "Marine Dues Bill" along with GST @ 18%. GST is charged by Ports for rendering "Port Services". The invoice issued by the Port for Port DA charges reflects the name of the Vessel carrying the cargo and the name of the steamer agent. Suppose ocean freight amount is Rs. 100 including PDA charges of Rs 20. Port Authorities charges GST on Rs. 20 as the service is provided in Indian Territory by the Port. GST on PDA charges is non-creditable as the vessel owner is a foreign party and does not have an output GST liability and hence is not in a position to claim input tax credit.

In case of import of goods, GST is payable under reverse charge by the recipient for transportation of goods by a vessel from a place outside India up to the customs station of clearance in India and tax credit of GST paid under reverse charge is available to importer. As mentioned above, in case of ocean freight the "Importer" has a liability to pay IGST under reverse charge. Ocean freight charges which is ultimately borne by the importer also includes the element of IGST paid by vessel owner on PDA charges and to this extent there is a double taxation of GST on PDA charges. The expenditure of IGST on PDA charges is expenditure in furtherance of business but importer is unable to get input tax credit of the same only due to the reason that direct payment for such charges has not been made by the importer. In view of the above, the IGST paid on the PDA charges is becoming a cost in the system. It is suggested that GST should not be levied on PDA charges to avoid double taxation or an appropriate mechanism should be devised to enable the importer to avail the tax credit of GST on PDA charges in the case of CIF import into India.

5.1.20. Procurement of HSD at concessional rate of CST

With introduction of GST in India, the definition of 'Goods' under section 2(d) of the CST Act has been amended to include only six items i.e. Petroleum Crude, High Speed Diesel (HSD), Motor Spirit, Natural Gas, Aviation Turbine Fuel, Alcoholic Liquor for Human Consumption. HSD is one of main input being used in Iron & Steel, Mining Industries and Power Plant. In previous tax regime, purchase of HSD at concessional rate of CST was permitted in CST Act, 1956. In GST regime, there is lack of clarity as to whether the items mentioned above can

still be purchased at concessional rate of CST, if conditions specified in CST Act, 1956 are satisfied.

In this regard, reliance can be placed on the decision of the Apex Court in the case of Printers (Mysore) Ltd. Vs. Asst. Commercial Tax Officer [1994] INSC 91 (7 February 1994) wherein it was held that Form C can be submitted for purchase of raw materials for production of newspaper which is outside the definition of goods (i.e. newsprint was excluded from definition of goods).

Presently, States are interpreting the law differently and there is a lot of ambiguity. Recently, one of the State has issued a notification where it has been mentioned that goods (as per the amended definition) can be purchased at concessional rate of CST only if such goods are used in manufacturing and processing of the same goods. For manufacturer of other items, mining industries and power plants the benefit will not be available as these industries have ceased to be dealer under the CST Act. Interstate or Intrastate Purchase of HSD without tax concession or Input Tax Credit involves huge cost in terms of Sales Tax and is going to significantly increase cost of finished goods. It will have an adverse impact on the domestic market and will also defeat the very objective of GST which has been brought in order to transform the country into a single common market.

Suitable steps should be taken by Government to ensure that benefit of purchase at concessional rate of CST is available.

5.1.21. Inclusion of Petroleum & Natural Gas within GST framework (including regasified LNG)

Petroleum products are an input to many industries and commercial activities. GST being applicable on the final product and not on the petroleum products which are inputs to the value chain defeats the purpose of GST.

Natural Gas being a cleaner fuel and the loss of tax revenue not significant. So Natural Gas must be immediately put under the GST ambit.

Petroleum products directly enter as an input into a large number of economic activities (e.g., transportation, electricity generation and fertiliser production). Apart from such direct uses, there are a number of indirect uses as well. Therefore, changes in prices (or taxes) of petroleum products would have a significant impact on the economy both through direct as well as indirect or cascading routes. The cascading overall impact on the other core sectors which are critical will be such that it would seriously impact the manufacturing competitiveness of India. Thus, increase in tax incidence would not only increase the Capital Cost of the Oil and Gas Sector but will also have an inflationary impact on the economy. In view of the above-mentioned adverse impact for non-inclusion of the Petroleum Products in GST regime, our request is as follows:-

All petroleum products such as petrol, diesel & natural gas should be immediately brought under the ambit of the GST regime. Non-inclusion of the same has pushed up costs for the sector. No input credit is available on goods and services used for petroleum operations. Denial of credits has resulted in massive cascading impact and increased cost of production

placing the domestic industry in a competitive disadvantageous position. This has an adverse impact on investments in this sector which is critical for energy self- sufficiency and import substitution.

It is recommended that oil and gas be included in GST regime, and thus, GST is levied on sale/supply of oil and natural gas. This inclusion will provide free-flow of credit and avoid cascading impact.

5.1.22. Reversal of input credit relating to Non-GST supplies be made nil

The provisions of the GST law require reversal of input tax credit in respect of exempted/non-taxable supplies. It would be unfair to compel a company to lose common credit merely because it has (non GST) trade turnover which may be more than 10 times higher than a service income merely for the same unit of measure due to the cost of the traded goods. This cost is of traded goods is not a value add of a trader and therefore should be excluded from the definition of turnover for comparing with a service income. This is akin to comparing the price of an air conditioner with the installation charges of an Air Conditioner by an AC dealer to its customer and denial of common credits on business costs of the AC Dealer. What is more reasonably comparable is the margin made by the dealer on the sale of the Air Conditioner with the installation charges for the Air Conditioner. From a combined reading of the various provisions of the GST Act it is evident that:-

- the exempt turnover includes non GST leviable category i.e. the petroleum goods
- turnover as it stands in the bill includes the cost of traded goods for a trading entity.

It is also being pointed out that including the petroleum goods as exempt category is unfair as VAT and Excise duties etc. continue to be applicable taxes on the manufacture and sales of these products. It is accordingly suggested that petroleum goods (being taxed separately) be excluded from the purview of exempt and total turnover under the GST laws for the reversal of credit.

5.1.23. Exemption from GST on import of vessel

In energy sector, vessels, tugs, barges etc. are imported by upstream companies or its vendors i.e. sub-contractors into India under charter-hire arrangements for specific period of lease. Import of vessel was exempted from payment of whole customs duty subject to Essentiality Certificate (EC) issued by Directorate General of Hydrocarbons (DGH). Under GST regime, though Basic Customs Duty and Customs Cess continues to be exempted, IGST of 5% is made applicable in terms of Entry no. 404 of Notification No. 50/2017 – Customs, dated June 30, 2017. In view of this Notification, IGST of 5% stands applicable on the assessable value of vessel, barge or tug at the time of its importation. In case where such vessel, tug or barges are imported by operators, sub-contractors or other vendors, such upfront payment of IGST @ 5% on assessable value of vessel, barge or tug leads to huge blockage of cash-flow for all importers. Also, in case where vessel, tug or barges are imported by sub-contractors or their vendors for shorter period of contract, the importers would not be in the position to claim credit of IGST paid since there would not be sufficient output GST liability. Such importers would be mandatorily required to opt for drawback or

export the same on payment of IGST and claim refund of the same. Import of vessel was exempted from payment of whole customs duty subject to EC issued by DGH in the Pre GST regime vide notification no. 12/2012- Customs. Such additional compliance coupled with huge blockage of cash-flow has already impacted operations of oil & gas companies. Further, where the same are imported by upstream companies, the amount of IGST paid less Drawback shall be a cost, leading to increased tax cost for oil & gas upstream sector. In case where vessel is imported for lease period of more than 18 months, drawback is also not admissible. It is suggested that Notification No. 50 / 2017 – Customs be amended to provide for complete waiver of IGST on import of all goods required for petroleum operations including tug, vessel and boats.

5.1.24. Exemption for O&G upstream companies for movement of goods from shore base to offshore

In case of oil & gas upstream sector, goods procured and kept at shorebase are supplied to offshore platforms as per indent. Subsequently, the same goods are supplied back to shore on real time basis on account of non-utilization/space constraint at offshore platforms. Again after few days/weeks, the same goods are required at offshore. Shorebase supplies the same goods to offshore again where IGST was paid during 1st dispatch. Under GST regime, shorebase and offshore location are distinct persons. Hence, on the basis of law, as it stands today, supplies from shorebase to offshore location would attract IGST. Hence, shorebase and offshore locations are required to issue tax invoice and pay IGST on its supplies to offshore location/shorebase, as the case may be, at the time of each supply. While this issue has been partly addressed vide Circular 21/21/2017-GST dated November 22, 2017 in so far it relates to inter-state movement of rigs, tools, spares and goods on wheels, taxability of movement of other shore base supplies (such as lubricants and other consumables) continues to be a concern.

Given this, such levy of IGST on supply of goods from shorebase to offshore location and backload therefrom should be exempted. Alternatively, in case where no upfront exemption is granted and first supplies from shorebase/offshore location are subjected to IGST of 5% once post introduction of GST, further supplies thereof from shorebase to offshore and backload therefrom to shorebase should be exempted without requiring reversal of credit. Such benefit of exemption if not conferred on such subsequent supplies between the same taxable persons i.e. shorebase and offshore platforms would mean levy of GST time and again on the same set of goods.

5.1.25. Admissibility of credit for O&G upstream companies – offshore registration in respect of goods being supplied back to shorebase after its use

In oil & gas sector, there would be multiple movement of goods from shorebase to offshore location and vice versa. Basis current legislation and credit mechanism on GSTN, it seems that offshore locations may not be allowed to claim credit of GST charged by shorebase since goods are used in exploration of oil & gas, which is outside the ambit of GST. Given this, while offshore locations may not eligible to claim credit of IGST charged by shorebase, offshore locations may be burdened with GST once again at the time of backload without credit. Such inconsistency would result into levy of GST again on the same goods as and

when they are supplied from shorebase to offshore and loaded back to shorebase. Further, such situation is against the principle of seamless flow of credit.

Option 1: Such levy of IGST on supply of goods from shorebase to offshore location and backload therefrom should be exempted.

Option 2: Alternatively, in case where no upfront exemption is granted and first supplies from shorebase/offshore location are subjected to IGST of 5% once post introduction of GST, further supplies thereof from shorebase to offshore and backload therefrom to shorebase should be exempted without requiring reversal of credit. Such benefit of exemption if not conferred on such subsequent supplies between the same taxable persons i.e. shorebase and offshore platforms would mean levy of GST time and again on the same set of goods.

Option 3: Offshore platforms should be allowed to claim credit of GST charged by shorebase to the extent of goods being back-loaded to shorebase. At times, the goods supplied to offshore platforms are returned to shorebase after lapse of considerable period. In such scenario, credit should continue to be allowed irrespective of its time limit.

5.1.26. Exemption Notification be extended to "All Goods and Services used for Petroleum Operations"

Notification No.3/2017-Intergrated tax (Rate) and Central tax (Rate) and State Tax (Rate) dated 28th June, 2017, cover only 24 items that would be subjected to Goods and Services Tax (GST) at the concessional rate of 5%. It may be noted that there is no distinction between goods and services as all the services (including capex expenditures services like drilling, cementing etc.) are utilised for carrying out exploration and production of oil and gas only. Exclusion of services from the exemption notification would be prejudicial to the interests of the oil industry and goes against the basic principle behind levy of GST**.** It is suggested that the exemption notification in this regard be suitably amended thereby enlarging the scope of the items to "all goods and services used for petroleum operations".

5.1.27. Denial of GST credit to customer, if supplier has defaulted in filing return

As per the provisions of the GST law, one of the conditions for availability of ITC is that the tax charged in respect of the supply has been actually paid to the Government by the supplier of goods and services. Further, if the supplier has defaulted in furnishing the details of outward supplies and the tax paid thereon, the customer will not be able to take the ITC in respect of such supplies. The basic premise of introduction of GST is to allow seamless flow of credit which seems to be defeated with the concept of recipient being made to suffer for the default of the supplier. Therefore, a review of the provisions of the GST laws considering the aforesaid aspect is needed. It is suggested that a suitable amendment be made in the GST laws to allow ITC to the customer in case he has made the payment of invoice along with tax to the supplier. Further, in such cases the supplier should be made liable to pay tax along with interest. This will protect the interest of the buyer and would also encourage the customers to do business with small and medium business units.

5.1.28. Cap Pre-deposit in case of filing appeal

Section 107(6) of the CGST Act provides for a pre-deposit of 10% of the tax in dispute for filing an appeal. Under the erstwhile regime, as per section 35F of the Central Excise Act, 1944, appeal against an order passed by the lower authorities is not to be entertained unless the appellant has made a pre-deposit of 7.5% in case of first stage appeal and 10% in case of second stage appeal, of the duty, where duty or duty and penalty are in dispute, or penalty, where penalty is in dispute. The total pre deposit under the section is subject to a ceiling of Rs. 10 Crores. This provision is effective from August 6, 2014.

The provision laid down in the CGST Act does not state any ceiling limit. It has been observed that in many cases huge demands are created arbitrarily against the taxpayer and the rate of success in appeal at CESTAT in favour of the taxpayer is very high. Mandatory payment of pre-deposit in all the cases that too without any ceiling limit will result in unnecessary financial hardship in the form of outflow of amount on account of pre-deposit. Since final disposal of the appeal takes time considering the pendency of the cases at CESTAT/Commissioner Appeals, the funds gets blocked for a long period of time. It is suggested that a cap of Rs. 10 crores be introduced in the GST law on the amount of pre-deposit in case 10% of the disputed tax exceeds Rs. 10 crores.

5.1.29. Allow credit in respect of demand confirmed after the July 1, 2017

As per the provisions section 142(6)(b) of CGST Act, 2017, if any amount of credit becomes recoverable as a result of appeal disposed of under the existing law the same shall be recovered as an arrear of tax under this Act unless recovered under the existing law and the amount so recovered shall not be admissible as input tax credit under the Act. This provision takes away the vested right of the assessee duly earned under the existing law and hence is against the common law of principle of equity. Even under the erstwhile regime, such credit was allowed unless the charges of fraud, suppression, etc. are upheld against taxpayer. It is suggested that the credit of payment made by the assessee against the CENVAT credit demand shall be allowed under the GST regime in cases wherein the charges of fraud, suppression, mis-statement of facts etc. are not proved. Appropriate amendment be made in the provisions of the GST laws accordingly. The provisions may be amended to restrict the non-availability of credit only if the charges of fraud, suppression etc. are upheld against the assessee.

5.1.30. Maintenance of Book of Accounts

Section 35(1) of CGST Act, 2017 prescribes that every registered person shall keep and maintain, at his principal place of business, as mentioned in the certificate of registration, a true and correct account of—

(a) production or manufacture of goods;

(b) inward and outward supply of goods or services or both;

(c) stock of goods;

(d) input tax credit availed;

(e) output tax payable and paid; and

(f) such other particulars as may be prescribed

Proviso to section 35 further provides that where more than one place of business is specified in the certificate of registration, the accounts relating to each place of business shall be kept at such places of business.

Under the GST regime, each taxable person has to take state-wise registration and each place of business of the taxable person in the state has to be added as place of business. In a large manufacturing organisation, there are multiple places of business in one state which includes factory, mines, depots etc. In such cases, it is not possible to maintain accounts at each place of business. Since there will be one registration in each state, there is no requirement to maintain the accounts at each place of business. Maintaining accounts at each place of business will require huge changes in the system of accounting which will ultimately impact the operation of the companies. It is suggested that the provision should be amended so as to provide for maintaining accounts at principal place of business only and not at all the place of business. This will promote ease of operation.

Given advancement in technology, the law may provide for maintaining only electronic records in each State, and physical records at Central office, to be produced for checking if and when required with reasonable notice.

Further as per rule 80 of the CGST rules, every registered person shall furnish an annual return in Form GSTR-9 in which details regarding profit as per profit and loss account, gross profit, profit after tax and net profit is required to be furnished. In a large company, profit and loss accounts are being maintained for the company as a whole. It is not possible to maintain profit and loss accounts and derive gross profit and net profit for each state. It is suggested that requirement of furnishing state-wise gross and net profits as per profit and loss accounts in annual return GSTR-9 should be removed.

Further, Rule 56(12) of the CGST Rules prescribes that every registered person manufacturing goods shall maintain monthly production accounts showing the quantitative details of raw materials or services used in the manufacture and quantitative details of the goods so manufactured including the waste and by products thereof.

In a large manufacturing organisation, there are many types of raw materials or services which are used directly or indirectly in the manufacture of a product. Hence keeping accounts of quantitative data of each raw material or service used in the manufacture will be extremely onerous. There is already plethora of details under the GST regime which are required to be uploaded by the taxpayer through upload of inward supplies, outward supplies coupled with matching concept for credits etc. It is believed that the requirement for further maintenance of accounts and records relating to raw material, finished goods, services etc. at such detailed level is extremely onerous and at the same time unwarranted.

It is suggested that the requirement of maintenance of production accounts for raw material and services, finished goods should be removed since GST is applicable on supply and not on manufacture unlike excise.

5.1.31. Non-Payment of consideration vis-à-vis output tax

As per the second proviso to the section 16(2) of the CGST Act, 2017, where the recipient fails to pay to the supplier the amount towards the value of supply along with tax payable thereon within period of 180 from the date of issue of invoice by the supplier, an amount equal to the input tax credit availed by the recipient shall be added to his output liability along with interest thereon, in such manner as may be prescribed. Some of the common prevailing and accepted trade practices regarding payment of the consideration for the supply and which are incorporated in the supply contract mutually agreed by the contracting parties are as follows:-

(i) Part of the consideration amount by way of retention money towards performance guarantee is paid at a later date on complying with the stipulated conditions.

(ii) Credit period in excess of 180 days from the date of raising invoice is provided by the supplier to the recipient.

(iii) Payment is guaranteed by way of Sight Letter of Credit (LC), in which case the supplier receives the payment immediately from the recipient's bank, but the same is debited to the recipient's account at a much later date.

(iv) Payment is guaranteed by banks by way of Usance LC, in which case the supplier receives the payment on a deferred date as per the agreed terms, but again the same is debited to the recipient's account at a much later date.

In all the above situations, even though the payment is not expressly made by the recipient within one hundred and eighty days, it cannot be said that he has failed to make payment within the said period. This provision will cause unnecessary hardship to the registered taxpayer who has withheld the payment because of valid reasons like towards performance guarantee/ quality of work as per the terms of contract.

It is suggested that necessary amendment be made in the second proviso to section 16(2) of the CGST Act to provide that input tax credit shall not be added to the output tax liability of the recipient in cases as may be prescribed even after the expiry of the period of one hundred and eighty days.

Section 140(9) of the CGST Act provides for re-claim of CENVAT credit on input services reversed in the earlier law subject to the condition that the registered person has made the payment of the consideration for that supply of service within a period of three months from the appointed date i.e. on or before September 30, 2017. It is suggested that the time limit of three months may be increased to 180 days from the appointed date to align it with the second proviso to section 16(2) of the CGST Act.

5.1.32. Clarify procedure for Refund of Cess

Section 9(2) of GST (Compensation to States) Act, 2017, provides that for all purposes of furnishing of returns and claiming refunds, except for the form to be filed, the provisions of the CGST Act and the rules made thereunder, shall, as far as may be, apply in relation to the levy and collection of the cess leviable under section 8 on all taxable supplies of goods or services or both, as they apply in relation to the levy and collection of central tax on such

supplies under the Act or the rules made thereunder. Forms and manner of claiming refund of compensation cess has not yet been prescribed.

It is accordingly suggested that forms and rules for refund of compensation cess must be prescribed at the earliest specifying time limit, form, manner etc.

5.1.33. Align provisions relating to time of supply - Reverse charge on goods and services

Section 12(3) of the CGST Act provides the in case of supplies of goods in respect of which tax is paid or liable to be paid on reverse charge basis, the time of supply shall be the earliest of the following dates, namely:-

a) the date of the receipt of goods; or

b) the date of payment as entered in the books of account of the recipient or the date on which the payment is debited in his bank account, whichever is earlier; or

c) the date immediately following thirty days from the date of issue of invoice or any other document, by whatever name called, in lieu thereof by the supplier:

Provided that where it is not possible to determine the time of supply under clause (a) or clause (b) or clause (c), the time of supply shall be the date of entry in the books of account of the recipient of supply.

Further 13(*3*) of the CGST Act provides that in case of supplies of services in respect of which tax is paid or liable to be paid on reverse charge basis, the time of supply shall be the earlier of the following dates, namely:-

a) the date of payment as entered in the books of account of the recipient or the date on which the payment is debited in his bank account, whichever is earlier; or

b) the date immediately following sixty days from the date of issue of invoice or any other document, by whatever name called, in lieu thereof by the supplier:

Provided that where it is not possible to determine the time of supply under clause (*a*) or clause (*b*), the time of supply shall be the date of entry in the books of account of the recipient of supply:

Provided further that in case of supply by associated enterprises, where the supplier of service is located outside India, the time of supply shall be the date of entry in the books of account of the recipient of supply or the date of payment, whichever is earlier.

In a large manufacturing company, following different process for reverse charge mechanism for goods and services will create difficulty in implementing the process. In case of goods, reverse charge mechanism arises at the time of receipt of goods whereas in case of services it is at the time of payment. The liability of tax in respect of goods and services should arise at the time of payment only. Appropriate amendment be made in the Act accordingly.

5.1.34. Issues - Work Contract Services

The Government has vide notification no. 20/2017 dated August 22, 2017 reduced the rate of tax on some of the work contract services from 18% to 12%.

However, the below mentioned work contract services have not been considered for exemption in the notification.

- Services by way of construction, erection, commissioning or installation of original works pertaining to airport, port, monorail or metro.
- Services provided by way of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation or alteration of a building owned by an entity registered under section 12AA of the Income Tax Act, 1961 and meant predominantly for religious use by general public.
- Services provided to the Government, a local authority or a governmental authority by way of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation or alteration of-

  (a) a civil structure or any other original works meant predominantly for use other than for commerce, industry, or any other business or profession;

  (b) a structure meant predominantly for use as (i) an educational, (ii) a clinical, or (iii) an art or cultural establishment; or

  (c) a residential complex predominantly meant for self-use or the use of their employees or other persons specified in the Explanation 1 to clause (44) of section 65B of the said Act;

The said services were exempted from service tax via mega notification no. 25/2012 – service tax dated June 20, 2012. It is accordingly suggested that the notification no. 20/2017 – Central tax (rate) be amended to include the aforesaid services within its scope.

It has also been observed that rate of tax on works contract services supplied to government, local authority or governmental authority by way of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation or alteration of (a) a historical monument, archaeological site or remains of national importance, archaeological excavation, or antiquity specified under the Ancient Monuments and Archaeological Sites and Remains Act, 1958 (24 of 1958); canal, dam or other irrigation works; pipeline, conduit or plant for (i) water supply (ii) water treatment, or (iii) sewerage treatment or disposal has been reduced from 18% to 12%. However, in construction industry for many of the reasons main contractor will use the services of a sub-contractor which will be subject to GST @ 18%. This will result in blockage of funds for the main contractor. It is suggested that reduction in rate should also be extended to sub-contractors. The refund provisions of the GST laws allows refund of unutilised input tax credit on account of rate of tax on inputs being higher than the rate of tax on output supplies, however, there is no provision to allow refund in respect of unutilised input tax credit in respect of input services. It is accordingly recommended that appropriate amendment be made in the GST law to allow refund of unutilised credit on account of rate of tax on input services being higher than the rate of tax on such outward supplies.

Some of the issues which further need to be addressed in case of works contract are given below:-

a) It is not clear whether executing a single contract for supply of goods and services with no split consideration would constitute as works contract or not. Clarity is also needed as to whether separate contract for goods and services or single contract for goods and services with split consideration would qualify as works contract. It is suggested that detailed guidelines/clarification be issued covering various contracting scenarios for a typical EPC contractor.

b) Goods such as JCB, Grader, Cranes, Dumpers, Tippers etc. qualify as motor vehicle under the Motor Vehicle Act. These goods are used for earth work, levelling etc. As per the provisions of the GST Law, input tax credit is not allowed on motor vehicles and other conveyances (except for making specified supplies). The aforesaid goods are capital goods primarily used for construction related activities by the EPC contractor and accordingly ITC on such goods should be allowed under the GST Law. It is suggested that appropriate amendment be made in the law to allow for credit on the aforesaid goods.

c) Section 31(5) of the CGST Act provides that in case of continuous supply of services the invoice shall be issued (a) where the due date of payment is ascertainable from the contract, on or before the due date of payment; (b) where the due date of payment is not ascertainable from the contract, before or at the time when the supplier of services receives the payment; (c) where the payment is linked to the completion of an event on or before the date of completion of that event.

   In case of contracts executed by EPC contractors, where the tenure for contracts exceeds the timeframe of three months, the supplies are treated as 'continuous supply of services'. In such contracts, payment is linked to certification of running account bill by the customer. Accordingly, invoices are raised on or before the date of customer certification. As per section 31(2) of the CGST Act read with Rule 47 of the CGST Rules invoice shall be issued within a period of thirty days from the date of the supply of service. However, provisions of section 13(2) of the CGST Act regarding time of supply of service mentions only about the invoice issued under section 31(2) of the CGST Act and does not refer to section 31(5) of the CGST Act. As a result, there is an ambiguity regarding the availability of period of thirty days for issuance of invoice in case of continuous supply of services. It is requested that appropriate clarity may be provided in this regard.

d) Under the foreign trade policy, supplies to mega power projects were entitled to deemed export benefits. However, under the GST regime, the supplies towards execution of power projects is liable to GST. Since the power companies are outside the ambit of GST they are not in a position to claim credit of tax paid on such supplies. It is suggested deemed export benefits may be extended to the supplies made to power project companies, especially to the existing notified projects.

5.1.35. Provide Clarity on GST on movement of goods acquired under operating lease

There is a practice of acquiring assets on operating lease for e.g. construction equipments by businesses. In case of operating lease/ hire of Plant & Machinery, possession & control is with the lessee and he is free to use it for any of his project across states. The lease rental/hire charges paid to Lessor are subject to GST. However, there is ambiguity whether the movement of such assets from one state to another will be classified as supply and is subject to GST. Appropriate clarity be provided in this regard.

5.1.36. Treatment of Sales Return

As per provisions of section 34(1) of the CGST Act, 2017, where the goods supplied are returned by the recipient, the registered person who has supplied such goods may issue a credit note to the recipient. The details of the credit note has to be furnished by the registered person in the return for the month during which such credit note has been issued but not later than September following the end of the financial year in which supply was made, or the date of furnishing of the relevant annual return, whichever is earlier. The tax liability of the supplier is to be adjusted accordingly. Practically, there would be number of cases where the goods sold would be received by the supplier after the last date of filing of annual return. As per the existing provisions of the GST laws, no adjustment from the output tax liability of the supplier would be allowed after the date of furnishing the annual return of the financial year. It is not reasonable to restrict the adjustment if goods are received by the supplier beyond a particular date. It is therefore suggested that appropriate amendment in the law be made to provide that adjustment shall be allowed to be made from the output tax liability of the supplier in the month in which the goods are returned and the details of the credit note issued shall be furnished by the person in the return of the month during which such credit note has been issued.

5.1.37. Classification Issues

There is a lot of ambiguity around classification of commodities under the GST regime. A particular item needs to be classified under 'Harmonised System Nomenclature (HSN) Code' on similar lines with Customs tariff for determination of applicable GST rate. Different interpretations on classification of items under HSN Codes are likely which is creating confusion for the taxpayers and the business operations of various industries are adversely affected. Clarity on classification of items and consequently the applicable GST rate is critical to ensure that the basic concept of GST being "one nation one tax" is not defeated. It is suggested that a proper mechanism (akin to constitution of a panel to resolve IT and export related issues) should be developed by the Government to resolve the classification and rates related issues at the earliest.

5.1.38. Abeyance of Penalty provisions for a period of six months

The introduction of GST signifies a major overhaul in the indirect tax regime of the country. It subsumes various central and state taxes and so is being called as one nation one tax. Filing of various applications, returns, forms etc. under the GST regime has been automated through a common portal viz. GSTN. Thus, successful operation of GSTN is the backbone for successful implementation of GST. With implementation of GST from July 1, 2017, not much

time was left with the trade and industry to get accustomed with the law. Coupled with this, various transitional challenges were faced by the taxpayers in uploading details on the GSTN, tracing of utilities etc. Considering that GST is completely a new regime of indirect taxes, there is a lack of awareness and ambiguity amongst the taxpayers on various issues. As a result mistakes in the initial few months are bound to occur. There is an apprehension that the taxpayer could be treated as a defaulter for non-compliance due to non-availability of certain filing utilities on the GSTN or due to technical glitch on the GSTN website. It is requested that for an initial period of six months from introduction of GST, implementation of the provisions relating to levy of penalty should be kept in abeyance.

5.1.39. Periodicity of GST returns

It has been observed that filing of monthly return under the GST regime coupled with monthly uploading of details of outward and inward supplies has added much to the compliance burden of the taxpayers. A lot of time and resources have been spent by the businesses in order to ensure compliance with the return filing deadlines under the GST regime which included filling of plethora of details, dealing with server issues, transitional credit claim issues and tracing of utilities on the GSTN portal etc. The Government decision requiring quarterly filing of returns by the small and medium businesses with annual aggregate turnover upto Rs. 1.5 crore in Form GSTR 1, 2 and 3 and also to discharge the tax liability on quarterly basis is welcome and would ease the compliance burden for the small taxpayers. Considering the time and resources involved in compliance under the GST regime and to ensure smooth transition to the GST regime it is suggested that the periodicity of filing of returns be made quarterly instead of monthly for all the taxpayers though payment of tax can be made monthly for taxpayers having annual aggregate turnover above Rs. 1.5 crores. This will simplify the compliance and will go a long way to boost the confidence of the taxpayers and encourage them to comply under the GST regime.

CUSTOMS

Procedures and Other Issues

5.2.1. Harmonisation of Customs Value and Transfer Pricing

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

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

5.2.2. Inverted Duty Structure – Indigenous Manufacture of Soap Noodles/Soap

Lauric Acid (HSN 2915 9090) is an essential ingredient for manufacture of soap noodles. It is sourced primarily from Malaysia and Indonesia and attracts Customs Duty @ 7.5%. Toilet and Soap Noodles and Soaps, on the other hand, attract 'Nil' Customs Duty under the aegis of the Indo-ASEAN FTA which covers several countries including Malaysia and Indonesia. Consequently, indigenous manufacture of soap noodles/soap has a higher tax cost than import of soap noodles/soap from ASEAN countries.

In order to provide a level playing field the Government, vide Notification No. 12/2014 – customs dated 11th July 2014 exempted Customs Duty on all goods (under HSN 3823 11,12,13 & 90 and 2915 70) used in the manufacture of soaps and oleo chemicals. However, Lauric Acid (HSN 2915 90) – a key ingredient of soap manufacture – was not covered by the said notification.

It is recommended that in order to eliminate the inverted duty structure by virtue of which indigenous manufacture of soap noodle / soap is more expensive than import of these goods from ASEAN, Lauric Acid (HSN 2915 70) may also be exempted from Customs Duty.

5.2.3. Allow imports of PE Resins at a concessional rate of duty [Mega Notification No. 12/2014]

Manufacturing industries in India are importing new PE Resin Technologies into India. The import of new resin is primarily being planned to reduce the plastic packaging thereby reducing the plastic waste and promoting environmental safety. These flexible packaging laminates are used in various manufacturing industries including FMCG for use in packing of finished products.

Borouge bimodal technology is unique in respect that it gives toughness to the packaging even after pack is down gauged. It reduces consumer and customer quality issues. The following three grades of resins are imported from Borouge UAE with HS Code 3901.90.90:

a. FB 2230 (Borstar technology bimodal LLDPE resin)

b. FB 1350 (Borstar technology bimodal LLDPE resin)

c. FK 1820 (Borstar technology bimodal Metallocene LLDPE resin)

It is submitted that appreciating the need for reducing the packaging footprint in the environment, efforts were taken to explore different technologies that can help industries to reduce the footprint. This further helps on protection of degrading natural resources and it is appropriate to country's context as it is environmentally effective, cost efficient, taking an integrated structured approach and avoiding barriers to trade. Overall, this would strive to reduce waste from manufacturing operations.

With the use of Borouge Bimodal technology industries can harmonize their flexible packaging laminate and also down gauge the material thickness. Reducing the material thickness has no negative impact on performance of the packaging if we use Borouge bimodal technology. In the second stage, efforts are on exploring the next level of resin change namely Metallocene grade, again using Borouge Bimodal technology. This

technology and products mentioned above would be used for manufacturing flexible packaging laminates which are generally used for medium and low income groups. Both these steps will help us reduce the amount of packaging by weight and will also result into lesser wastages which would ultimately be a step towards environmental friendliness.

It does not result into any kind of damage to the quality of product for which such packaging material would be used.

Middle East traditionally has lowest cost of Polyethylene resin and Asian countries like India has the best cost of converting the resin into film. It's a perfect match and surely suits the current theme of "Make in India" as the country can then use them domestically and / or export the finished polyethylene film to any part of the world at a very competitive price. Currently the above mentioned grades attract 7.5% Basic Custom Duty.

None of the Indian manufacturers have this "Borouge Bimodal technology" and therefore, if the duty is reduced or exempted on these resins, it would not have any adverse impact on the domestic manufacturing sector.

It is further stated that that these types of resins are also manufactured in Singapore where Indian Government has given the preferential duty treatment under India- Singapore FTA. It is requested that import of the aforesaid resins be subject to zero basic custom duty subject to condition that these resins would be utilized for manufacturing, of flexible packaging laminates required for manufacture of products listed in the IEM of the respective manufacturing industries. The actual user condition can be monitored by the revenue department as to the actual use of these resins into specified packing materials. The manufacturing of end products can be checked by monitoring the IEM's and therefore, the necessary system to check the use of resins for manufacturing of packing material for specified end products is already in place. It is believed that granting of this concession would go a long way in promoting environmental safety thereby reducing packaging foot print.

5.2.4. Removal of cess on customs duty

As a rationalization measure, the education cess and secondary and education cess leviable on excise duty had been fully exempted. Suitable amendments may be made to fully exempt education cess and secondary and education cess leviable on customs duty.

5.2.5. Duty free import of oils for manufacture of soaps/oleo-chemicals under conversion arrangement

Oils such as Palm Fatty Acid Distillate [PFAD], Stearine, Stearic Acid, etc. are converted into Distilled Fatty Acid [DFA] and DFA is subsequently used for the manufacture of soaps. Such oils (only with FFA content of more than 20%) are allowed at `nil' rate of duty as per Sr. No. 230A of the Notification No.12/2014-Cus dated 11.7.2014 read with Customs [Import of Goods at Concessional Rate of Duty for Manufacture of Excisable Goods] Rules, 2016 when imported into India for manufacture of soaps and oleo-chemicals.

One of the conditions for import of the industrial oils under concessional rate of duty is prior permission from the Jurisdictional Central Tax Authorities for import of such oils and such

permission/certificate obtained should be submitted to Customs authorities at the time of filing the Bill of Entry for allowing duty free clearance.

While there has been no issue in case of manufacturing activities undertaken at the own unit the problem arises when such manufacturing activities are contracted to a third party who undertakes the manufacturing activity for and on behalf of the brand owner/principal manufacturer who supply the material.

Although two legal entities are involved in the process of importing and conversion of oils into DFA for manufacture of soaps the ownership in the goods shall always remain with principal manufacturer [importer].

The Customs Act and/or Central GST Act, 2017 do not define the term "Actual User". The Foreign Trade Policy (FTP), which regulates imports and exports, defines "Actual User (Industrial)" in Para 9.5 of Chapter 9, as under:-

"Actual User (Industrial)" means a person who utilizes the imported goods for manufacturing in his own industrial unit or manufacturing for his own use in another unit including a jobbing unit."

From the above, it is clear that if the imported goods are utilized for manufacture of the final products in his own unit and/or in a jobbing (job-worker's) unit, it would be treated as fulfilment of "end use". The benefit given under the aforesaid notification cannot be taken away mere because of involvement of two entities and on account of certain procedural difficulties. The solution lies in taking an undertaking from the original importer in order to safeguard the interest of the revenue and also ensure that the oils so imported are used only for manufacture of soaps/oleo-chemicals. The notification does not impose any restriction for the conversion arrangement and it only stipulates the condition of end use which stands fulfilled by virtue of the arrangement as elaborated above.



Federation of Indian Chambers of Commerce and Industry

Federation House, Tansen Marg, New Delhi 110001
Phone: +91-11-23738760-70 (Extn.- 574)
Fax: +91-11-23721504/23320714
E-mail: ira.khanna@ficci.com
Website : www.ficci.com