cl!ent alert

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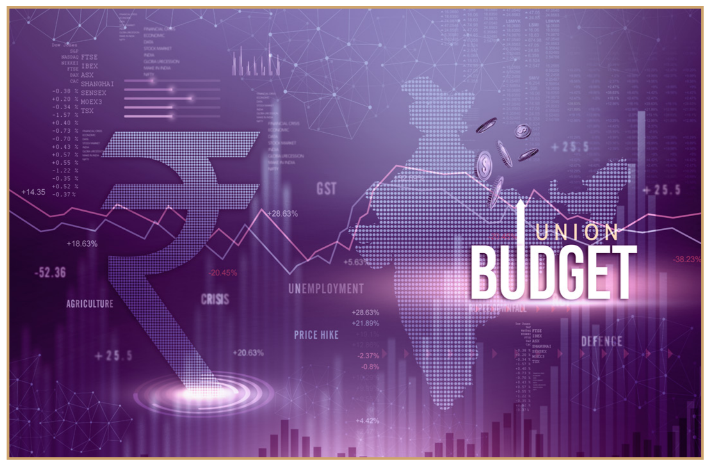
ahead of the curve

Union Budget 2021: Budget Highlights

At the outset



The Finance Minister (“**FM**”) had the unenviable task of delivering on her promise of a never-before-seen budget this year. She and her team worked under extremely challenging times: the GDP having shrunk into negative in fiscal 2020-21 due to obvious adversities faced by the economy reeling under the pandemic. She has acted deftly and with confident boldness, which is exemplary and laudable. The FM focused on growth while taking a calculated risk on widening fiscal deficit. She announced major reforms, to take effect with certain new legislations, rules and regulations. Not increasing any direct taxes is a major positive. Instead, as mentioned in her speech, the fine print of the Finance Bill, 2021 (“**Bill**”) demonstrates plugging of several loopholes and removing some uncertainties for more efficient tax administration. Levy of agri cess under indirect tax is a clever stroke. Everyone dealing in those goods will pay the cess but it is not slapped on foreign investors if they are not subject to indirect tax, which majority of private equity, investment funds and foreign portfolio investors (“**FPIs**”) are not. And yet, it is likely to result in higher collections! Some of the measures announced under the Income-tax Act, 1961 (“**IT Act**”) for senior citizens, individual taxpayers, etc., are very welcome. For instance, no advance tax shall be payable on dividend income unless the dividend is declared and accrued. Reducing the reopening of assessment to three years in normal cases is a key amendment. Significant reduction in time limit from twenty-one months to nine months for completion of assessment would go a long way in reducing uncertainty. Settling the withholding tax rate for FPIs by providing that treaty rates will apply, would remove the anxiety created by a recent Supreme Court decision.

To provide a shot in the arm to the disinvestment and privatization program, it is proposed that brought forward losses in case of public sector strategic divestments and amalgamations or demergers will be available for future set off. Removing levy of dividend withholding tax for Real Estate Investment Trusts (“**REITs**”) and Infrastructure Investment Trusts (“**InvITs**”) coupled with expanding the class of assets to qualify for InvITs will go a long way in restoring the attractiveness of monetizing infra-assets.

Creation of ‘bad bank’ to address the issues of non-performing assets of banks and improve their fiscal health has been an ask of the entire financial sector. The FM has made a major announcement in this regard of creating an Asset Reconstruction Company and Asset Management Company, which will buy out the stressed loan portfolios of banks and Alternative Investment Funds (“**AIFs**”) would in turn be able to invest in them. If structured carefully and managed professionally, this can produce the desired results. Moreover, the proposal to allow foreign control / majority shareholding of up to 74% in insurance companies will not only promote foreign investments in the sector but also enable insurance companies to tap into an important capital source, thereby ensuring they remain afloat during these stressful times.

While a lot of unique and much-needed measures have been announced, this was the time to also make a bold statement of removing the causes of international tax disputes which have emerged due to the retrospective change in law for taxation of indirect transfer of Indian assets. Hopefully, soon, provisions will be brought in to provide tax certainty in case of offshore listing of Indian companies and the much talked about Special Purpose Acquisition Corporations, looking to infuse the huge investible funds available offshore. The dispute resolution mechanism which is proposed to be provided to small companies can be extended to ALL companies involved in cross border transactions and especially non-resident taxpayers.

On balance, it is fair to say that the FM has lived up to her claim to announce a unique budget. It can be fairly stated that there is something in it for everyone. It certainly generates confidence in the economy and the policymaking initiatives of the government as well as paves the way for a five trillion-dollar economy.

This client alert gives a glimpse of the major fine print provisions set out in the Bill.

Yet another shout out to IFSC units!

The IT Act provides various concessions to units situated in the International Financial Services Centre ("**IFSC**"). With the intention to create a 'world-class financial services centre' in IFSCs, the Bill proposes further incentives as follows:

1. Relaxation of eligibility criteria for investment funds

The IT Act contains a beneficial regime to promote offshore funds being managed from India, subject to certain eligibility criteria. In order to attract the management of investment funds from an IFSC, the Bill proposes that the government may by way of a Notification relax the eligibility conditions for the investment fund and fund managers to benefit from the exemption of taxable presence in India by way of business connection, under section 9A of the IT Act. These benefits are proposed to be extended to fund managers which have commenced operations in the IFSCs on or before March 31, 2024.

2. Relaxation for investment divisions of offshore banking units located in IFSC

The IT Act provides that Category III AIFs located in IFSC are exempt from tax on capital gains arising from the transfer of certain specified securities to the extent they pertain to the units held by non-resident investors. In order to attract relocation of offshore banking units in IFSCs, the Bill proposes to extend the aforementioned exemption to investment divisions of banking units of a non-resident located in IFSCs and which have *inter alia* been registered as a Category III AIF.

Further, the Bill also proposes to amend the IT Act to provide that, subject to such conditions as may be notified, the income derived by a non-resident from the transfer of non-deliverable forward contracts entered into with offshore banking units of an IFSC, shall be exempt. The Bill also proposes to extend the beneficial regime for taxation of income from securities and capital gains under section 115AD of the IT Act, as applicable to FPIs, to such investment divisions of offshore banking units as mentioned above.

3. Tax exemption for relocation of funds

In order to encourage various foreign funds to relocate their operations to IFSCs, the Bill proposes various relaxations. It proposes that any income in the nature of capital gains arising to a non-resident, which is on account of transfer of shares of a company resident in India pursuant to relocation of a fund incorporated outside India to IFSC, shall be exempt from tax under the IT Act. For the purpose of these provisions the transferor fund means a fund incorporated outside India, which collects funds from its members for investing it on their behalf and fulfils certain prescribed conditions. Further, it is required that such funds transfer their assets, on or before March 31, 2023, to a fund located in an IFSC centre, which satisfies certain prescribed conditions. Furthermore, the consideration for the transfer of assets is required to be rendered in the form of units or interest in the recipient funds to the shareholder/unit holders of the transferor fund, in the same proportion in which they held units or interest in the transferor fund.

It is also proposed to amend the IT Act to provide that any gain arising from transfer of any capital asset pursuant to the aforementioned relocation of funds would not be subject to capital gains tax. Similarly, it is also provided that any gains arising from the transfer of units or interest, held as capital assets, by unitholder/shareholders of the transferor fund, pursuant to the aforementioned relocation of funds, would also be exempt from capital gains tax. Bill also proposes certain other amendments in this regard to exempt such transfers from fair valuation norms, restrictions placed on carrying forward of losses pursuant to change in shareholding etc.

4. Incentives for IFSC units engaged in aircraft leasing activities

The Bill proposes certain changes to the IT Act in order to attract more investors setting up IFSC units engaged in aircraft leasing activities. The existing section 80LA of the IT Act provides for profit linked deduction on the gross total income of the unit of an IFSC. The deduction is 100% of the income derived by such unit for its business which has been approved for setting up the unit in IFSC. The Bill proposes to amend the IT Act so as to exempt income arising from the transfer of aircraft or an aircraft engine, which was leased by an IFSC unit to a domestic company engaged in the business of aircraft operation, provided the unit has commenced its operation on or before March 31, 2024.

Further, the Bill proposes to exempt royalty income of a non-resident on account of lease of aircraft paid by IFSC units, if the unit commences its operation on or before March 31, 2024.

These amendments are proposed to be effective from April 1, 2021.

Investment funds

'Zeroing' in on infrastructure

Infrastructure Debt Funds ("**IDFs**"), incorporated and registered as non-banking financial companies, are currently allowed a 100% tax exemption under the IT Act, subject to certain conditions. This mandates that the IDF shall only issue rupee-denominated bonds or foreign currency bonds in accordance with the directions of the Reserve Bank of India ("**RBI**") and the relevant foreign exchange regulations, and not zero-coupon bonds, which are non-interest paying bonds that are issued at a deep discount and redeemed at face value. The cost of discount at which such zero-coupon bonds are issued, is permitted as a deductible expense currently to the issuer of zero-coupon bonds, provided that the issuer is an infrastructure capital company, infrastructure capital fund, public sector company or scheduled bank. While RBI permitted IDFs to issue such bonds, the deduction in respect of discount for zero-coupon bonds under the IT Act was not permitted to them. The Bill now rectifies this by permitting IDFs to issue the qualifying zero-coupon bonds. The proposal is expected to provide a great boost to the availability of funds for the infrastructure sector.

The amendment is proposed to be applicable from April 1, 2021.

Business trusts are made sweeter for equity investments

Post Finance Act, 2020 dividend income is directly taxed in the hands of shareholders, at the rate applicable to them; and the company distributing the dividends is required to withhold tax at the prescribed rates. REITs and InvITs (collectively referred to as "**Business Trusts**") are exempt from tax on dividend income received from a special purpose vehicle ("**SPV**"), i.e., an Indian company in which the Business Trust holds controlling interest or such percentage holding, as may be prescribed.

Even though the dividend income is exempt in the hands of Business Trusts, no specific exemption had been granted to the SPVs from withholding tax obligation while distributing to Business Trusts. In order to rationalise this and remove unnecessary hassle for the Business Trust, the Bill proposes to carve out an exemption from withholding tax on dividends paid by an SPV to a Business Trust.

This should have a positive impact on the attractiveness of Business Trusts, both in case of real estate and infrastructure investments.

These amendments are proposed to be effective retrospectively from April 1, 2020.

Removing cause of conflict in withholding tax for FIIs

Currently, the IT Act provides tax deduction at source at the rate of 20% on income from securities to a Foreign Institutional Investor ("**FII**") (other than income in respect of certain bonds and government securities). The provision does not use the words 'at rates in force' for applying the withholding tax rates. The definition of 'rates in force' includes within its purview, the rates under the applicable Double Taxation Avoidance Agreement ("**DTAA**"). This lacuna resulted in creating confusion that the intention may not be to apply the rates under the applicable DTAA to the FIIs in respect of such income from securities. The Bill proposes to clear this confusion and provide that the tax would be deducted at source at the rate of 20% or any lower rate under the applicable DTAA, where the FII furnishes the tax residency certificate for claiming relief under the applicable DTAA.

This is a welcome clarification, though it is applicable prospectively, from April 1, 2021.

Taxability of sovereign wealth funds and pension funds rationalized

Currently, the IT Act provides for exemption from income-tax to certain sovereign wealth funds ("**SWF**") and pension funds ("**PF**") on income in the nature of dividend, interest or long-term capital gains arising from investments made by them in India. For availing this exemption, SWF/PFs need to fulfil certain conditions.

The Bill proposes to rationalize the existing provisions and remove some practical difficulties pertaining to the conditions they need to fulfil. Some of the key changes are highlighted below:

1. **Investment into a Category-I or Category-II AIF**

   Currently, the AIF in which the SWF/PFs invest is required to make 100% investment in an eligible infrastructure company. This is found to be restrictive. It is hence proposed to change this as follows:

   a. The AIF would be required to invest at least 50% in infrastructure companies.

   b. The AIF can invest in an InvIT.

   c. Exemption under this clause shall be calculated proportionately if the aggregate investment of AIF in infrastructure company or companies or in InvIT is less than 100%.

2. **Investment through a holding company**

   The Bill proposes to permit SWF/PFs to make investments through an Indian holding company structure subject to such holding company having a minimum of 75% investment in one or more infrastructure companies where such a company is set up on or after April 1, 2021. Exemption under this clause shall be calculated proportionately, where the aggregate investment of holding company in infrastructure company or companies is less than 100%.

3. **Investment in NBFCs, etc.**

   The Bill proposes to permit SWF/PFs to make investments in non-banking finance companies registered either as infrastructure debt funds or infrastructure finance companies which have a minimum 90% lending to one or more of the infrastructure companies or enterprises. Exemption under this clause shall be calculated proportionately, where the aggregate lending of these companies in infrastructure company or companies is less than 100%.

4. **Relaxation for leveraging by SWF/PFs**

   Currently, SWF/PFs are not allowed to have loans or borrowings or deposit or investments since one of the conditions for the tax benefits provides that no benefit should enure to a private person. It is proposed to provide that there should not be any loan or borrowing for the purpose of making investment in India. It is also proposed to provide that the condition of no benefit to private person and requirement of assets going to the government on dissolution would not apply where payment is for repayment of loan taken for purposes other than investing in India.

5. **Relaxation for commercial activities by SWF/PFs**

   Currently, SWF/PFs cannot undertake any 'commercial activity' in or outside India if they seek to avail the tax benefit in India. This condition is proposed to be removed and replaced with a condition that SWF/PFs shall not participate in 'day to day' operations of investee entities. In this regard, it is also clarified that if the SWF/PFs appoints a director and executive director for monitoring the investment, that would not amount to participation in day-to-day operation of the investee company.

6. **Taxability of PFs in home countries**

   Currently, it is provided that a PF would be eligible for the tax exemption in India only if it is not liable to tax in its home jurisdiction.

   However, it is found that some PFs are liable to tax in their home country though they are subsequently exempted from tax. It is proposed to amend this condition to provide that if the PF is liable to tax but exemption from taxation for all its income has been provided by the home country under whose laws it is created or established, then such PF shall also be eligible for the benefits available to SWF/PFs under the IT Act.

   These proposed amendments should expand the investor population in this category for the huge funds required in the infrastructure sector.

   These amendments are proposed to be effective from April 1, 2020.

Business reorganisation – no more unintended benefits

Depreciation on 'goodwill' – Denied!

There is considerable litigation around the issue of availability of depreciation on 'goodwill' arising from transactions pertaining to merger, demerger, business acquisitions, etc. The Supreme Court in the case of **Smiff Securities Limited (2012) 348 ITR 302 (SC)** had ruled that goodwill is an intangible asset and if acquired as a result of an acquisition transaction would be eligible to depreciation.

The Bill proposes that goodwill of a business or profession will not form part of a block of assets in any situation, thereby denying depreciation on it. Where goodwill is purchased by a taxpayer, the purchase price of the goodwill will be considered as 'cost of acquisition' for the purpose of computing capital gains on the sale of such goodwill. Such 'cost of acquisition' shall be reduced by the depreciation claimed by the taxpayer on such goodwill prior to financial year 2020-21, i.e., before this provision is brought into effect. The Bill proposes to make several consequential amendments in the definition of 'capital asset', section 32 which deals with the depreciation of assets, meaning of the term 'cost of acquisition', etc., to give effect to the above changes.

As this amendment is proposed to be effective from April 1, 2020, to that extent, it is retrospective.

Slump exchange – Taxable

Currently, any transfer of an undertaking as a result of 'sale' for a lump sum consideration is regarded as 'slump sale' for the purposes of the IT Act and liable to capital gains tax. There has been considerable disagreement on whether a transfer of an undertaking for consideration in kind instead of cash would qualify as a 'slump sale' and hence, be subject to capital gains tax. Certain judicial rulings have held that a transaction would be liable to capital gains tax, if it is for cash consideration and not if it is for exchange of assets.

The Bill proposes to plug this loophole by amending the definition of 'slump sale' by providing that "transfer" of an undertaking 'by any means' (and not just limited to transfer by way of sale) would amount to slump sale. This brings a slump exchange within the tax net. The term 'transfer' in this section is given the same exhaustive meaning as under section 2(47) of the IT Act, i.e. to mean sale, exchange, relinquishment, etc.

This amendment is proposed to be effective retrospectively from April 1, 2020.

Plugging the loopholes in partnership reconstitution

Currently, the IT Act imposes capital gains tax in the hands of the partnership firm at the time of distribution of assets on the dissolution of the firm or "otherwise". It has been interpreted that this tax does not apply in case of reconstitution of partnership. The Bill proposes to extend this taxability to the reconstitution of a partnership firm. Further, the Bill also proposes to levy similar capital gains tax in the event money or other assets are distributed to the partners in excess of the balance in their capital account.

In this regard, the Bill proposes to clarify that for the purpose of computation of the capital gains on the partnership firm, the fair market value of the capital or other asset or the value of cash, as the case may be, on the date of the receipt by the partners, shall be deemed to be the full value of consideration. In addition, in the event of distribution in excess of balance in the capital account, the capital account balance of the partner at the time of the dissolution or reconstitution of the firm would be considered as the cost of acquisition. The Bill further clarifies that this balance shall not take into account, increase in the capital account of the partner due to revaluation of any asset or due to self-generated goodwill/other asset. Therefore, any surplus on the revaluation is now proposed to be taxed under the IT Act. It may be noted that income from such distributions at the time of dissolution or reconstitution would typically not be eligible to treaty benefits since this tax is on the partnership, which would be an Indian tax resident.

This amendment is proposed to be effective retrospectively from April 1, 2020.

Start-ups and MSMEs rejoice! Tax holidays and benefits extended

Currently, an eligible start-up is entitled to a tax holiday for three consecutive years out of the first seven years of its incorporation or registration. The tax holiday could be availed only by companies or limited liability partnerships incorporated or registered before April 1, 2021. This deadline for incorporation is now proposed to be extended to April 1, 2022, in order to allow more new start-ups to benefit from the tax holiday.

The extant provisions allow for capital gains from the sale of residential property to be invested in eligible start-ups/ MSME and the start-up/MSME in turn utilising the capital infusion for purchase of a new asset, in which case, the transferor of the residential property is entitled to special capital gains exemptions depending on the value of the asset as against the consideration received for the residential property. To avail this exemption the residential property must be transferred before April 1, 2021. In order to invite capital investments in start-ups and pump much-needed liquidity into the manufacturing MSME sector, this deadline is proposed to be extended to April 1, 2022.

These amendments are proposed to be applicable from April 1, 2021.

Corporate tax and TDS

Tax to be deducted at source on purchase of goods

The Bill proposes to introduce a new provision which obligates every person making payments to a resident taxpayer for purchase of goods, to deduct tax source at the rate of 0.1% of the payment exceeding INR 5 million. The liability to deduct tax has been imposed only on those persons whose gross receipts or turnover exceeds INR 100 million in the year preceding the year in which the goods are purchased. Further, the government is empowered to notify classes of taxpayers where these provisions may not apply.

It is also proposed that such obligation to deduct tax at source would not apply if tax is required to be deducted under any other provision of the IT Act or if tax is required to be collected at source under the IT Act. However, if a transaction is subject to the provision relating to tax collection at source under section 206C(1H) as well as tax deduction at source under this provision, then the proposed provisions relating to tax deduction would apply.

Further, the Bill proposes to empower the government to issue guidelines to remove any difficulties. Additionally, the IT Act is also proposed to be amended to provide that if the seller fails to furnish his PAN, then the tax under these provisions would be deducted at the rate of 5%.

These amendments are proposed to be effective from July 1, 2021.

Non-filers of returns to pay TDS and TCS at higher rates

In order to ensure that taxpayers timely file their income tax returns, the Bill proposes to introduce two new sections, which propose to deduct tax at source and collect tax at source, respectively, where the taxpayers have not filed their income tax returns.

The Bill proposes to insert section 206AB, which provides for a higher rate of tax deduction under specified provisions of the IT Act, from payments made to a specified person. Subject to certain other conditions, a specified person is defined to mean a person who has not filed income tax returns for the last two years preceding the year in which tax is to be deducted. Tax would be deducted under these provisions at the higher of the following (i) twice the rate specified in the IT Act; (ii) twice the rates in force; or (iii) 5%.

The Bill proposes to introduce similar provision under section 206CCA in relation to tax collection at source.

Clearly, the government wants taxpayers to be vigilant about tax compliances and wants to ensure that the tax base is widened.

These amendments are proposed to be effective from July 1, 2021.

Rationalizing the provisions of Minimum Alternate Tax

Under the current provisions, Minimum Alternate Tax (“**MAT**”) is levied at the rate of 15% on the book profits, as computed under the Companies Act, 2013, subject to certain adjustments provided under the IT Act, if the tax liability under the normal provisions of the IT Act is less than 15% of the book profits. Currently, the IT Act does not provide for any adjustment on account of any incremental income resulting from secondary adjustment made under the IT Act or pursuant to any advanced pricing agreements. Unlike in case of interest, capital gains, FTS, royalty etc., dividend income received by a foreign company, may be included in its book profits in the event such company pays tax at a concessional rate under the applicable DTAA.

Pursuant to various representations made by the stakeholders, it is proposed to amend the MAT provisions such that dividend income shall not be included in the book profits, in case of a foreign company where such income is taxed at a rate lower than MAT pursuant to the DTAA.

The Bill further proposes to amend the IT Act to provide that where the book profits of the taxpayer increase due to inclusion of past year income on account of an advance pricing agreement or secondary adjustment, then the tax officer may on an application made by the taxpayer, compute the book profits of the past years and tax payable, in the prescribed manner, thus, providing clarity to the taxpayers.

These amendments are proposed to be effective from April 1, 2020.

Changes in tax audit thresholds – promoting digital transactions

Currently, every person carrying on a business with total sales, turnover or gross receipts over INR 10 million is required to have his/her accounts audited by an accountant before the specified deadline. Vide the Finance Act, 2020, a relaxation was carved into this requirement whereby businesses with up to INR 50 million of total sales, turnover or gross receipts were exempt from this requirement if the aggregate receipts and payments in cash during the year did not exceed 5% of the aggregate receipts or payments, respectively. The Bill proposes to increase the total sales, turnover or gross receipt threshold for such non-cash-based businesses to INR 100 million. This achieves a two-fold objective: incentivising non-cash transactions and reducing audit compliance burden for small and medium enterprises.

The amendment is proposed to be applicable from April 1, 2020.

Real estate

Homing in on 'Housing for All'

In furtherance to the objective to achieve 'Housing for All', the government vide Finance Act, 2016 provided 100% deduction to builders and developers of affordable housing projects in respect of profits and gains derived from such affordable housing projects. The deduction was available on the satisfaction of certain specified conditions, including, *inter alia*, a condition that such housing projects should be approved by the competent authority between June 1, 2016 and March 31, 2021 (extended from March 31, 2020 vide Finance Act, 2020). To provide a further boost to affordable housing, the Bill proposes to extend the period of approval of such housing projects by competent authority till March 31, 2022. Further, the Bill extends the tax holiday to builders and developers of affordable rental housing projects notified for this purpose by the government on or before March 31, 2022. This last proposal is aimed at facilitating affordable housing for migrant workers.

To augment the purchasing power for affordable housing, the Bill proposes to extend the benefit of deduction of INR 1.5 lakh to home buyers on the loans sanctioned by financial institutions till March 31, 2022.

These amendments are proposed to be applicable from April 1, 2021.

Shot in the arm for real estate

The IT Act has inbuilt safeguards against the transfer of undervalued immovable property. For the purpose of computing capital gains tax, section 43CA deems stamp duty value ("**SDV**") assessed by the appropriate state government authority for any land or building or both, to be the full value of consideration. This was relaxed to not attract SDV value where the SDV is not more than 110% of the actual consideration.

The safe harbour provided under this provision is proposed to be increased from 10% to 20% for first-time homebuyers who purchase residential units between November 12, 2020 and June 30, 2021, for a consideration of less than INR 20 Million.

Similarly, section 56 of the IT Act taxes recipients of immovable property for less than fair market value as 'other income' on the difference between the SDV and the consideration paid if such difference is more than 10% of the consideration or INR 50,000, whichever is higher.

The safe harbour under section 56 is proposed to be increased from 10% to 20%. With the COVID-19 tremors still rocking asset prices, this move is intended to boost real estate demand to help the sector.

These amendments are proposed to be applicable from April 1, 2020.

Tax administration related changes

Disputes Resolution Committee to target the untapped

Recognizing the need to ease tax compliance and addressing tax uncertainty in the face of tax disputes, the Bill proposes to introduce a new scheme to provide early tax resolution to small and medium taxpayers. To complement the existing schemes for settlement of existing tax disputes, the Bill proposes to constitute one or more Disputes Resolution Committee ("**DRC**"), which would resolve disputes arising from fresh assessments, where the returned income is INR 5 million or less (if any) and the proposed addition/variation is less than INR 1 million.

The Bill proposes to exclude orders which are based on search or survey proceedings or exchange of information under DTAA or Tax Information Exchange Agreements from the scope of this scheme. Subject to certain conditions to be prescribed, the Bill proposes to give the DRC the powers to reduce or waive penalty under the IT Act or grant immunity from prosecution for any offence under the IT Act in case of a person whose dispute is resolved under this scheme. The Bill proposes that taxpayers in respect of whom an order of detention, prosecution or conviction under various laws has been made or instituted, would not be eligible to claim the benefit of the proposed scheme under DRC. Similar to faceless assessments and appeals, the Bill proposes to empower the central government to make a scheme by notification in the official gazette with the aim to impart greater efficiency, transparency, and accountability by eliminating interface to the extent technologically feasible.

These amendments are proposed to be effective from April 1, 2021.

Faceless ITAT proceedings to be the new face of the appeals process

With the faceless assessments and appeals and penalty mechanism in place, the government is continuously striving to pave way for further transparency, and accountability in the tax dispute redressal mechanism. To further reduce the physical interaction between the taxpayers and adjudicating authorities, the Bill proposes to introduce a faceless scheme for proceedings before the ITAT. In this regard, the Bill proposes to enable the central government to notify a scheme for disposal of appeal by the ITAT, increase transparency, efficiency, and accountability by eliminating physical interaction between the ITAT and parties to the appeal and introducing an appellate system with dynamic jurisdiction.

These amendments are proposed to be effective from April 1, 2021.

AAR reform: heralding a new era

The Authority for Advance Rulings ("**AAR**") has been functioning as an alternate forum for non-residents and qualifying residents to seek clarity on their present and potential tax obligation. However, of late, the efficacy of the AAR has dwindled considerably. The Supreme Court has often condemned the AAR for far exceeding its allotted time of six months for disposing of cases – recent reports suggest the average disposal time of the AAR has been four years. The posts of Chairman and Vice-Chairman of the AAR, where only retired judges of the Supreme Court or High Court can be appointed, have often remained vacant. Noting that the working of the AAR has been seriously hampered and that there is a need to provide an alternative route for timely advance rulings to taxpayers, the Bill proposes to abolish the AAR with effect from a date to be notified and in lieu, constitute the Board of Advance Ruling ("**Board**") exclusively for the purpose of determinations or rulings in respect of the IT Act.

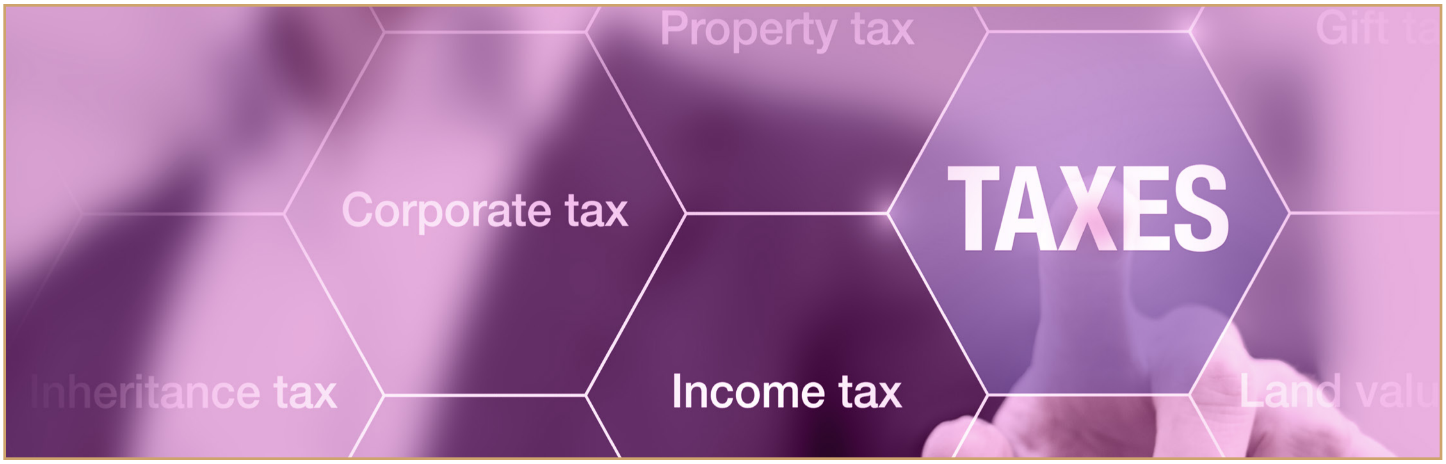
Multiple Boards are proposed to be constituted, each of which shall consist of two members, being officers not below the rank of Chief Commissioner. The Board's advance rulings are proposed to not be binding on the applicant or the revenue, unlike the AAR's rulings which are binding qua the applicant and the revenue, and not on other taxpayers. Appeals are proposed to be allowed against the Board's rulings to the jurisdictional High Court. With the notification of the Boards, all pending AAR proceedings will be shifted to the respective Boards. It is targeted that Board proceedings shall soon be brought under the revenue's expanding faceless administration scope. The Board, as is the case with the AAR, is required to pronounce its rulings within six months of receipt of an application. While this is a welcome development for expediting the resolution of issues of taxation, the concern is that the entire mechanism falls within the Department of Revenue and is no longer independent as it is meant to be under the extant AAR regime.

The amendment is proposed to be applicable from April 1, 2021.

Settlement Commission de-commissioned!

Currently, the Income-tax Settlement Commission ("**ITSC**") has the power to deal with settlement of cases involving assessments pursuant to search or requisition. In line with the proposal to overhaul the assessments/re-assessments in search, requisition etc., the Bill proposes that the ITSC shall cease to operate on or after February 1, 2021 and an Interim Board may be constituted to address the pending applications. The Bill proposes that no fresh application for settlemenst of cases shall be made on or after February 1, 2021. Where, applications in respect of which an order is pending before the ITSC on or before January 31, 2021, they can be withdrawn at the option of the taxpayer, failing which it shall be allotted or transferred to the Interim Board for adjudication.

These amendments are proposed to be applicable from February 1, 2021.



Demystifying the Vivad se Vishwas Act, 2020

The Vivad se Vishwas Act, 2020 ("**VsV Act**") was enacted with effect from March 17, 2020 with an aim to reduce the pending income tax litigation. The Bill proposes to clarify that the term 'appellant' under the VsV Act, shall not include any person in whose case there is any special leave petition, writ petition or any other proceeding arising out of an order of the ITSC is pending or has been disposed of.

This amendment is proposed to be applicable from March 17, 2020.

Shrinking of time of uncertainty for completion of assessments and re-assessments

Currently, the IT Act provides for a period of twenty-one months from the end of the relevant assessment year for the completion of assessment. The Finance Act, 2017 had reduced this period to eighteen months for Assessment Year 2018-19 and twelve months for Assessment Year 2019-20 and subsequent assessment years. It is now proposed to reduce this time period to nine months, thereby significantly reducing the period of uncertainty.

The Bill also proposes to reduce the time limit of six years for issuance of notice for reassessment to three years, unless there is evidence with the tax officer for income escaping assessment of INR 5 million, in which case the time limit for issuance of notice for re-assessment would be ten years from the end of the relevant assessment year.

These amendments are proposed to be effective from April 1, 2021.

India further hardens its stance on taxing digital economy transactions – Equalization Levy

The Finance Act, 2016 as amended by Finance Act, 2020 had expanded the scope of the Equalization Levy and made it applicable to the consideration received or receivable by an e-commerce operator from e-commerce supply or services made or provided or facilitated, by the former. The Bill proposes that the 'consideration received or receivable' shall include the consideration for the sale of goods, irrespective of whether the e-commerce operator owns the goods, and consideration for the provision of services irrespective of whether the e-commerce operator provides or facilitates such service. The Bill thankfully proposes to clarify that 'consideration received or receivable' shall not include consideration which is taxable as royalty or FTS under the IT Act read with the applicable DTAA. This would avoid the confusion and overlap in the existing provision.

Currently, the E-commerce supply or service is defined to mean:

i. online sale of goods owned by the e-commerce operator;

ii. online provision of services provided by the e-commerce operator;

iii. online sale of goods or provision of services or both, facilitated by the e-commerce operator; or

iv. any combination of activities listed in above clauses.

The Bill proposes that online sale of goods and online provision of services shall include one or more of the following activities taking place online:

i. Acceptance of the offer for sale;

ii. Placing the purchase order;

iii. Acceptance of the purchase order;

iv. Payment of consideration; or

v. Supply of goods or provision of services, partly or wholly.

These amendments are proposed to be applicable retrospectively from April 1, 2020.

Currently, the provisions of the IT Act exempt income arising from e-commerce supply or services made or provided or facilitated on or after April 1, 2021 which is chargeable to Equalization Levy. Though the Equalization Levy as introduced by the Finance Act, 2016 read with Finance Act, 2020 was applicable from April 1, 2020, the exemption is available in respect of services provided or facilitated on or after April 1, 2021. The Bill proposes to clarify and make good the anomaly with respect to this exemption, and provides that income arising from e-commerce supply or services made or provided or facilitated on or after April 1, 2020 which is chargeable to Equalization Levy shall be exempt from tax under the IT Act.

These amendments are proposed to be applicable *retrospectively from April 1, 2020.*

Disinvestment of PSUs strategized for additional funding

Tax proposals on the concept of demerger

The aftereffects of COVID-19 on the Indian economy have undoubtedly created need for more finances with the government In line with the suggestions of industry champions and experts, the government has taken a bold step to fill some of the fiscal gap with much talked about strategic disinvestment of public sector undertakings.

This also needed some tax facilitation, which has been proposed in the Bill. Currently, the IT Act provides for set-off and carry forward of the unabsorbed depreciation, and accumulated loss of amalgamating company in the hands of the amalgamated company if the amalgamating company is *inter alia* a public sector company engaged in the operation of aircraft, subject to certain conditions. The Bill proposes to extend this benefit to *inter se* amalgamation of one or more public sector companies without regard to the nature of the business carried out by the amalgamating company.

The Bill also proposes to extend this benefit to the amalgamated company, if the share purchase agreement under strategic disinvestment restricted immediate amalgamation of the said public sector company, and such amalgamation takes place within five years from the end of the FY in which such restriction ends. Strategic disinvestment for this purpose, is proposed to be defined as sale of shareholding by the government, which reduces its shareholding to less than 51%, along with transfer of control to the buyer.

Similar to the above benefit in case of amalgamation, currently, the IT Act enables set-off and carry forward of unabsorbed loss or depreciation of demerged company subject to certain conditions. The Bill proposes to extend these benefits by deeming reconstruction or splitting up of a public sector company into separate companies to be a demerger, if:

i. such reconstruction or splitting up has been made to transfer any asset of the demerged company to the resultant company;

ii. the resultant company is a public sector company on the appointed date indicated in the scheme; and

iii. fulfils such other conditions as may be notified by the central government.

These amendments are proposed to be applicable from April 1, 2020.

Proposals related to Stamp Act

With the view to remove hurdles to the government's grand disinvestment plans, it is proposed to amend the Indian Stamp Act 1899, to provide that any strategic sale, demerger, disinvestment, etc., of immovable property by a government company, its subsidiary, unit or joint venture, to another government company or to the central government or any state government, after the approval of the central government, shall not be liable to stamp duties.

Non-residents and Individuals

Ray of sunshine for taxpayers with income from overseas retirement funds

Taxpayers who are resident in India face hardship with respect to Indian taxation at the time of withdrawal from overseas retirement funds, in which they had contributed while they were non-residents of India. This hardship is caused since withdrawal from such funds is taxed in India on an accrual basis, while the foreign country may tax such funds on receipt basis.

The Bill proposes to amend the IT Act so that income of resident taxpayers from certain specified accounts situated in prescribed countries, shall be taxed in the manner as notified by the government provided such account was opened by the taxpayer in such prescribed country when he/she was non-resident in India and resident of that country.

These amendments are proposed to be effective from April

1, 2021.

Clarifying the scope of 'liable to tax' under the recent stateless person rule of tax residency

Through the Finance Act, 2020, a new section was added to the IT Act whereby Indian citizens are deemed to be Indian tax residents if they were not 'liable to tax' in any other country by reason of domicile or residency or any other criteria of similar nature. This position is regardless of whether such individual met the 182-day and related residency tests under section 6. The undefined term 'liable to tax' was a subject of heavy discussion owing to conflicting judicial precedents.

The term 'liable to tax' is now proposed to be defined as those persons on whom there is a liability of tax under the law of any country for the time being in force. It also clarifies that it would include a person who is liable to tax under the law but has been subsequently exempted from such tax.

The term 'liable to tax' also finds mention in the residency clause of multiple DTAAs. The Bill proposal implies that DTAAs will now squarely cover those entities which are liable to tax in the respective contracting states and have been granted exemptions under the tax laws thereunder, such as certain sovereign wealth funds, government-owned investment companies or banks, employment benefit funds, etc.

These amendments are proposed to be applicable from April 1, 2020.

No interest on shortfall in advance tax on account of dividend income

With the abolition of dividend distributions tax, dividend received from Indian companies is taxable in the hands of the shareholders at the applicable rates. Accordingly, taxpayers who are required to pay advance tax under the IT Act are required to estimate dividend income while determining the advance tax payable. As per section 234C of the IT Act taxpayers are liable to interest at the rate of 1% per month for a period of three months on the amount of shortfall of the advance tax instalments. Section 234C of the IT Act also provides for certain relaxation from payment of interest, subject to certain conditions, in cases where an accurate determination of advance tax is not possible due to the inherent nature of the income (e.g. capital gains).

Recognising that it would not be possible for shareholders to accurately estimate dividend income for the purpose of computing advance tax, the Bill proposes to amend section 234C to include dividend income in the aforementioned exclusions. Thus, under the new proposal, no interest would be payable on any shortfall in advance tax, where the shortfall is on account of dividend income, subject to such tax being subsequently paid in full. However, it would be relevant to note that proposed relaxation is not applicable in respect of loan or advance made by a closely held company to its shareholder which are deemed to be dividend under section 2(22)(e) of the IT Act.

These amendments are proposed to be effective from April 1, 2020.

Customs

Tariffs

1. The Bill seeks to provide the much-anticipated thrust to the domestic market by revising rates and reviewing existing exemptions. Major sectors impacted include:
    a. Automobile parts
    b. Chemicals
    c. Gems and Jewelry
    d. Electrical and electronics
    e. Agriculture
    f. Textile
    g. Plastics
2. ***Agriculture Infrastructure and Development Cess ("AIDC")***: The Bill introduces AIDC with effect from February 02, 2021. AICD will be imposed at rates ranging from 1.5% to 100% on the import of specified goods in the agricultural, alcohol, thermal, etc. sectors. AIDC is to be used to finance the improvement of agriculture infrastructure and other development expenditure.

3. ***Social Welfare Surcharge*** (“**SWS**”): The Bill also withdraws the levy of concessional SWS on import of gold and silver with effect from February 02, 2021. It exempts SWS on the value of AIDC imposed on gold and silver. It also rescinds the levy of SWS on import of crude or roughly trimmed or blocks of marble or travertine.
4. ***Health Cess***: Levy of Health Cess is exempted with effect from February 02, 2021 on the import of medical devices by international organizations and diplomatic missions to India.
5. ***Withdrawal of redundant exemptions***: The government also rescinded various exemption notifications which were no longer relevant or had become redundant such customs duty exemption on goods imported for organizing FIFA under 17 world cup; tags and labels, or printed bags of foreign origin imported for repairs and return; certain items of machinery for setting up of solar generation facility, etc.
6. The Bill also includes substantive proposals on provisions pertaining to safeguard, countervailing duty and antidumping duty with a view the corresponding to strengthen the investigation proceedings and regulations in line with best international practices. Proposals include amendments permitting retrospective imposition of countervailing/ antidumping duty to counter circumvention; imposition of circumvention/ antidumping duty on goods imported by EOU or SEZ units; anti-absorption measures, etc.

Trade Facilitation

1. ***Introduction of a Common Customs Electronic Portal*** (“**CCEP**”): In a bid to go paperless, the Bill contemplates notification of a CCEP to act as a single digital of interface between the trade and the customs department. CCEP would facilitate registration, filing of bills of entry (“**BoE**”), shipping bills, other documents and forms prescribed under any other law or rules or regulations, payment of duty and any other customs processes notified by the Central Board of Indirect Taxes and Customs (“**CBIC**”). Service of notice, order or any communication under the Customs Act, 1962 (“**Customs Act**”) is also proposed to be made through the CCEP.
2. ***Amendment of customs documentation on CCEP***: Presently, any amendments to documents presented at the customs house can be made only upon approval by the concerned customs officer. The Bill proposes to permit importer or exporters to make amendments to such documents on the CCEP. Permission to make such amendments would be granted electronically based on risk evaluation through an appropriate selection criterion.
3. ***Advance filing of Bill of Entry made mandatory***: To reduce dwell time, the Bill mandates filing of BoE for goods by the end of day preceding the day of their arrival at the customs station for clearance for home consumption or warehousing. The CBIC would be empowered to prescribe a different timeline (not exceeding the date of arrival of the goods) in presentation of BoE for specific cases.
4. ***Customs (Import of Goods at Concessional Rate of Duty) Rules, 2017 (“IGCR”)***: IGCR are amended to expressly allow 100% job-work on materials (except gold and jewelry and other precious metals) imported under concessional rate of duty for manufacture of goods on job-work basis. Even imported capital goods used for the specified purposes are permitted to be cleared on payment of differential duty, along with interest, on their depreciated value.

Tighter Control and Efficiency Mechanisms

1. ***Expiry date for exemptions***: The Bill proposes that all conditional exemptions granted under the Customs Act would stand rescinded on March 31 following two years after the date of such grant unless specified otherwise.
2. ***Timebound assessments***: The Bill proposes to impose prospectively a time limit of two-year (extendable further by one year by the Commissioner) for completion of any proceedings initiated under the Customs Act which would culminate in the issuance of a show cause notice for recovery of duty or interest short paid or unpaid or erroneously refunded.

3. ***Widened power to confiscate export goods***: The Bill proposes to introduce a new provision that would make any goods liable to confiscation where they are entered for exportation by making wrongful claim of remission or refund of duty or tax or levy in contravention of the provisions of any law in force.
4. ***Imposition of penalty on utilization of fraudulent credit***: The Bill also contemplates imposition of penalty in cases where a person has obtained any invoice by fraud, collusion, willful misstatement or suppression of facts to utilize Input Tax Credit ("**ITC**") based on such invoice for discharging any duty or tax on goods that are entered for exportation under claim of refund of any duty or tax.

Goods and Services Tax ("GST")

1. ***Scope of supply***: The Bill proposes to amend the Central GST Act, 2017 ("**CGST Act**") retrospectively with effect from July 01, 2017 to effectively tax supplies of services/ goods between a person (other than an individual) such as clubs and associations and its members. For this purpose, an explanation would also be inserted to state that the person and its members are deemed to be two separate persons. The relevant entry in Schedule-II would be omitted.
2. ***ITC restriction***: The Bill proposes that ITC on procurements would be available to the recipient only where GSTR-1 (i.e. return of outward supplies) is filed by the supplier and the supplies get reflected in GSTR-2A (i.e. auto-generated purchase return) to the recipient.
3. ***Relaxation in filing of annual return***: The Bill contemplates removal of mandatory requirement of filing reconciliation statement duly audited by specified professional and provides for filing of the annual return (GSTR-9) on self-certification basis.
4. ***Interest on cash liability***: The Bill proposes to amend the CGST Act retrospectively with effect from July 1, 2017 to provide for levy of interest only on net cash liability of the taxpayer in case of delayed payment of tax.
5. ***Increase in the amount of pre-deposit required to file an appeal***: The Bill proposes to increase the amount of pre-deposit for filing an appeal against an order

passed for payment of penalty for release goods and/ or conveyances detained under section 129 from 10% to 25% of the penalty imposed.
6. ***Scope of zero-rated supplies***: The Bill proposes to amend the Integrated GST Act, 2017 to include under the ambit of zero-rated supplies only those supplies to SEZ unit/developers which are made for their authorized operations. Proposals also provide that where a supplier making zero-rated supplies is unable to realize the sale proceeds within the period prescribed, such supplier would be liable to be pay back the ITC obtained as refund along with interest. Also, unlike the present provisions which entitle all registered persons to pay tax on zero-rated supplies and claim refund; the amendments propose to restrict such facility only to specified classes of notified persons or supplies.

Central Excise

1. In order to counteract the imposition of AIDC on petrol and high-speed diesel, the excise duties have been calibrated so that there is no additional burden on the consumer.
2. Other changes in the excise rates include addition of new tariff items under 2404 (i.e., products intended for inhalation) with the duty rate of 81% and NCCD of 25% with effect from January 1, 2022, as well as tariff rate of 14% + INR 15.00 per litre on automotive diesel fuel and fuel blend effective retrospectively from January 1, 2020.

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