# TAXATION

There are number of proposals contained in the Finance Bill every financial year, for amendments to be made in the Income-Tax Act. Many proposals are sought to be given retrospective effect having adverse impact on the assesses or on the efficient functioning of the tax administration. Such amendments create genuine hardships to the taxpayers and the same also affects financial projections of the assesses in respect of the past periods. Such taxation acts also encourage tendency of lack of accountability and disregard for the statutory provisions in the Tax Administration which is not good in the long run.

## I.1 Direct Taxes

There is need to enhance tax revenue by broadening the tax base and increase efficiency of tax administration. Tax regimes need to be modernized and focused on a customer service approach. The Government needs to bring an atmosphere of mutual trust and faith between the tax administrators and tax payer:

### I.1.1 Personal Tax

**Tax Slab**

Assesses having income less than Rs. 10,00,000 need to be taxed at 5% and 10% in two slabs rather than 10% and 20% as at present. The maximum marginal rate can be reduced to 25%.

**Finance Act 2013 Section 80EE**

Provides Rs 1-lakh deduction for interest payable by individuals taking new home loans up to Rs 25 lakh between April 1, 2013 and March 31, 2014 to buy their first residential property.

**Suggestions:**

To continue with Section 80EE for the fiscal year 2016-17.

### I.1.2 Corporate Tax

Surcharge at 10% for domestic companies and 5% for foreign companies (such as branches of foreign companies) where total taxable income exceeds Rs 10 crore to be retained.

**Suggestions:**

- To maintain the tax structure to achieve the fiscal deficit targets.
- The tax rates applicable to foreign companies must be brought at par with the rates applicable to domestic companies.
- Valuation of shares is highly litigated by the Indian transfer pricing authorities and it is also challenged by the regulatory authorities. As the new government is keen on liberalizing foreign direct investment (FDI) guidelines to attract additional investments, it is imperative to have consistency in the methods followed for valuation of shares under the tax provisions and under the Exchange Control Regulations.

- Currently, a taxpayer is not considered as a defaulter for non-deduction or short deduction of taxes in respect of payments made to an Indian resident, where the resident pays taxes on that income, files a tax return considering the said income, and furnishes a certificate from an accountant. Similar benefits should also be extended to payments made by a taxpayer to a non-resident subject to compliance of the conditions provided.

**I.1.3 Dividend Distribution Tax**

Surcharge at 10% on dividend distribution tax for large dividend tax-paying companies such as ONGC, Coal India, TCS, ITC, NTPC to name a few.

**Suggestions:**

- To maintain the tax structure to meet the fiscal deficit targets.

**I.1.4 Minimum Alternate Tax**

Removal of MAT has been a long standing issue of the industry there have been demands from various quarters to discontinue MAT. The Government proposes to rationalize all deductions and reduce corporate tax to 25 %.

**Suggestion:**

- The provisions of minimum alternate tax may be dropped from AY. 2016-17.

**I.1. 4(a) Amendment of Section 80-IA regarding upgrading existing infrastructure**

Infrastructure development is a pre requisite for the growth and development of any country. It is either to build altogether new infrastructure or to convert the existing structure by upgrading it and also enhancing the existing capacity. Both activities entail huge investment and human efforts.

It is recommended that a suitable amendment may be made in the Act to clarify that the up-gradation/extension of the existing infrastructure facility would also be eligible for the benefit of Section 80-IA of the Act.

**I.1.4 (b) MAT on infrastructure companies**

Minimum Alternate Tax is applicable to all infrastructure sectors such as roads, ports, power, telecom and railways. Infrastructure sector is the backbone of the Indian economy and the development of Infrastructure helps stimulate economic growth. Roads, ports, power, telecom, railways are the engines of economic growth. This sector is also highly capital intensive and requires large investments in the initial years. MAT imposes further burden on the tax liability of the infrastructure projects and erodes their profitability

Government has offered various tax incentives under Section 80-IA of the Act to the infrastructure companies to boost infrastructure. The benefit available to the infrastructure companies under the normal provision of the Act get neutralized since the companies are required to pay MAT on their book profit.

**Suggestions:**

- Considering the key role played by the infrastructure sector in the economy, the sector may be exempted from the purview of MAT.
- Benefit of carry forward losses including depreciation to be fully given in all stages before imposing MAT. Artificial disallowances in this regard need to be done away with. MAT on SEZ needs to be scrapped.

### I.1.4 (c) Rate of MAT and AMT

Presently, the rate of MAT/AMT is 18.5%, whereas the normal corporate tax rate is 30%; the minimum rate of 18.5%is almost 61.67% of the normal rate.

**Recommendations:**
The rate of MAT/AMT be reduced to 10%, so that the tax actually represents the "minimum tax"/ "alternative tax".

### I.1.4 (d) Corresponding deduction under MAT:

The tax incentives provided under these sections get neutralized on account of the companies being subject to tax under MAT.

**Recommendations:**
All the aforesaid deductions should be allowed while computing the book profits which will be subject to MAT.

### I.1.5 Transfer Pricing (TP) - domestic and international

### I.1.5 (a) Harmonising and reducing the unwanted compliance burden:

The Finance Act 2012 has introduced DTP in spite of existing provisions under the law which empower the tax authority to disallow unreasonable expenditure incurred between related parties (section 40A) or recompute the income of tax payers availing of profit-linked deductions, if there are transactions with related parties or other undertakings of the same tax payer (see sections 80A, 80-IA, similar Chapter VI-A deductions or section 10AA). These transactions are presently benchmarked against fair market value.

**Recommendations:**
Harmonization of the "Related Party" definitions:  Presently, three different sections referred to in section 92BA and section 92A of the law have different thresholds for the determination of the 'Related Party' definitions' which are as follows:

Substantial Interest – Not less than 20% of voting power –Explanation (b) to section 40A(2);

Associated Enterprises - Not less than 26% of voting power – section 92A(2)(a) & (b);

Associated Person - Not less than 26% of voting power – section 80A read with section 35AD(8).

There is clearly a need for the harmonization of the different thresholds for the 'Related Party' definitions in the sections and necessary amendments in this regard should be carried out.

Presently, there is no guidance in respect of benchmarking of the directors' remuneration. Since payment of directors' remuneration is subject to DTP provisions, necessary guidance for benchmarking it should be provided. It is further suggest that there should be no restrictions on directors' remuneration based on profits computed within the limits as specified under the companies law.

Arm's Length Price vs. Ordinary Profits: section 80IA(8) deals with "ordinary profits" whereas transfer pricing compliance refers to the "arm's length price" of the transactions. Conceptually, "price principles" cannot apply for the benchmarking of "profits".

Currently, there is no provision relating to correlative adjustment in DTP. It is very important that in any case covered under the DTP provisions, if any adjustment [upward or downward] is made, then a correlative adjustment in the hands of the other party should invariably be made. There are no methods prescribed for such correlative adjustments and the existing ones are not well equipped to deal with the issues of DTP. Necessary amendments should be made in the DTP provisions to provide for the correlative adjustments.

Exclusion of expenditure of a capital nature: The term specified domestic transaction has been defined to mean any expenditure in respect of which a payment has been made or is to be made to a person referred to in clause (b) of sub-section (2) of section 40A. Such an expenditure could include capital expenditure made to such a related person, even though section 40A(2)(b) does not apply to capital expenditure. It is therefore suggested that it should apply to expenditure referred to in section 40A(2)(a), and not to payments made to persons specified in section 40A(2)(b).

In respect of specified domestic transactions, the TP regulations, if at all, should be restricted to determining the comparable uncontrolled price method prescribed under section 92C.

**I.1.5 (b) AMT on all persons other than companies**

**Need for dilution of the threshold:**

By introducing Chapter XII-BA (sections 115JC to 115JF), from AY 2012-13, LLPs are treated like companies, with the difference that LLPs are taxed on adjusted total income, being the income determined under the provisions of the law before considering deduction available for SEZs and deductions available under Part C of Chapter VI-A (instead of taxation on the basis of the book profits, which is applicable to companies).

**Recommendations:**
Further AMT has been made applicable to all non-corporate entities except an individual or a Hindu Undivided Family (HUF) or an Association of Persons (AOP) or a Body of Individuals (BOI), or an artificial juridical person whose adjusted total income does not exceed Rs. 20 lakh. This limit is inadequate and should at least be equated to Tax Audit turnover limit under section 44AB of Rs.1 crore.

### I.1.5 (c) Section 115-O – DDT - Granting credit to the shareholders:

The DDT on companies has effectively been increased from 17% to over 20%.

The issue regarding non-creditability is an important issue and especially relevant to cross border investments i.e. foreign companies investing into Indian companies, because in all fairness, they should get a credit in the home country (this does not have any negative revenue impact for India).

**Recommendations:**
It must be clarified that the DDT paid by the company is deemed to be tax paid by the investor thereby making it possible for the taxpayer to claim credit; this will also enable foreign companies to claim credit in their home countries without impacting Indian revenue.

Disallowance envisaged under section 14A should not be made because, DDT is effectively a tax paid by the shareholder and there is no reason to deny him the deduction for expenses and interest that he may have incurred in making these investments.

Also, the rate of DDT needs to be reduced.

Section 32AC/ 35(2AB)/ 35AD deductibility under MAT

### I.1.6 Alternative Investment Fund (‘AIF’)

Finance Act, 2015 has changed the taxation regime of AIFs falling under Category I and Category II by providing them partial pass-through status. section10(23FBA) read with section 115UB provides that any income of AIFs other than income chargeable under the head ‘Profits and gains of business or profession’ would be exempt in the AIF’s hands and be taxable in hands of the investors on a pass-through basis.

The characterization of income from investments in securities as capital gains or business income has always been a vexed issue with only guiding principles provided in a CBDT instruction/ circular. In absence of a clear provision to treat AIFs’ income as capital gains, there is high probability of tax authorities characterizing the gains from investments by AIFs as ‘business profits’, thereby taxing the AIFs income at the fund level, i.e., effectively, no tax ‘pass-through’ section 115UB provides that net losses incurred by the AIF would not be passed on to investors, i.e., loss can be carried forward and set off only at AIF level. This will result in additional tax outflow for investors who could have used the loss as a set-off against their individual taxable income. Additionally, losses of the AIF remaining to be set off at the end of its term would lapse on winding down/ liquidation.

Further, section 194LBB provides for withholding tax at 10% by the AIF on the income (other than income taxable at AIF level) payable to investors. This will result in tax being withheld on exempt incomes like long term capital gains on listed securities on which STT has been paid, dividend and buyback proceeds. In case of non-resident investors availing benefit under the DTAA, the tax withholding will result in a cash trap. Further, where an investor in the AIF is also an AIF, it would lead to multiple levels of withholding tax.

**Recommendations:**
Characterization of income- Business income vis-à-vis capital gains - Clarity should be provided on characterization of income earned by AIF from investment activity. As the primary objective of AIF is to make investments, and not to engage in business activity, income earned by it from investment activity should be regarded as being in the nature of capital gains. This could be achieved by amending the definition of capital asset under section 2(14) to include investments held by AIF in accordance with the applicable regulations of Securities and Exchange Board of India.

Carry forward and set-off of losses - Delete section 115UB(2) to extend tax 'pass through' to losses. Alternatively, provide that unutilised losses of the AIF on liquidation shall be passed on to the unitholders.

**I.1.6 (a) Category 3 AIFs should also be covered under the amended tax regime.**

Withholding tax on distribution of non-business income – Amend section 194LBB to exclude tax withholding on the following income payable to investors:

- Any exempt income, like long term capital gains on listed securities on which STT has been paid, dividend, buyback proceeds.
- Income subject to beneficial treatment under the DTAA (withholding to be applied based on provisions of the DTAA, where more beneficial).
- Income payable to an investor who is an AIF.

Also, tax withholding on distributions to non-residents should be governed by section 195 so that tax would be deducted on only those incomes which are taxable in India.

**Other recommendations:**
- High pitched assessments and forceful recoveries of Tax demands.
- It has become routine to make huge additions and disallowances and forceful recoveries are being made to achieve the revenue collection targets. This causes tremendous hardship as well as disturbance in business. Therefore, the instructions of the board should be followed in the true spirit and a sympathetic approach should be taken for the grant of stay particularly, in respect of high pitched assessments.

- As a matter of internal control such high pitched assessment may be reviewed at Commissioner of Income Tax (CIT) / Chief Commissioner of Income Tax (CCIT) level. A track should be kept of the fate of such additions / adjustments at the Appellate level.
- Non grant of refunds or not completing rectifications
- It is common practice that rectifications are not carried out in particular when they are likely to result in refunds, and the tax payers have to keep running from pillar- to- post to get the refunds.
- Similar situations occur of not granting appeal effects etc. Strict instructions as well as regular monitoring at CIT level will help to avoid such hardships to the tax payer. It is not always possible for the tax-payer to keep complaining to the superiors.
- Harshness and high-handedness in handling TDS matters
- The tax payer is doing an honorary duty in assisting government for the collection of tax and depositing with them. If there are any ambiguities in the interpretation of provisions, immediate clarifications should be issued by the concerned Commissioner or the CBDT. For mistakes on account of interpretational issues, penal and harsh action should not be taken against the tax-payers, who are doing honorary work for the government.
- It has also been noticed that several notices have been sent to tax-payers to showcase why prosecutions should not be launched against them for delays in payment or on account of short payments (including on account of interpretation of provisions of TDS).
- Issues related to TDS and section 197 certificates
- There has been a considerable delay in issue of section 197 certificates which has caused serious cash flow issue for various payees.
- Strict timelines as listed in the Citizens Charter for the issue of section 197 certificates, should be adhered to, and time lines for approvals of files by the senior officers should also be laid down.
- Rejection orders should not be on frivolous grounds and a well speaking order should be passed.
- There should be a proper checklist of all the documents required to be filed along with the application.
- Where the certificate has been issued in earlier years, a certificate for subsequent years, in the absence of any change of facts, should be expedited and should be issued within two weeks from the date of application.
- Dispute Resolution Panel (DRP) and other Appellate issues
- Appeal against the directions and power of DRP to enhance variations – sections 144C & 246A

**I.1.6 (b) Needless litigation:**

Under the amended provisions of the mechanism of the DRP, the Income Tax Department will now have a right to appeal against the directions of the DRP. Furthermore, the new explanation introduced in Finance Act 2012 with retrospective effect states that the DRP will have the powers to enhance variations and shall always be deemed to have included the power to consider any matter arising out of the assessment proceedings relating to the draft assessment order, irrespective of whether the matter was raised by the tax payer or not.

When introduced, the intention behind the DRP mechanism was to reduce prolonged litigation and achieve quick settlement of disputes. However, allowing the Income Tax Department to appeal against the directions of the DRP would result in increased and prolonged litigation and would result in the defeat of the main purpose of its introduction. Furthermore, the amendment proposing to grant powers of enhancement will also result in increased litigation. There would then be no material difference between the appeal before the CIT(A) and the DRP and it would not result in any alternate dispute resolution mechanism.

**Recommendations:**
Accordingly, so that the main intention of creating an alternate dispute resolution mechanism is not defeated, the Income Tax Department should not have the right to appeal against the directions of the DRP. Furthermore, the DRP should not have the powers of enhancement.

**I.1.6 (c) Provisions quite broad-based need to be restrictive:**

Finance Act, 2015 amended section 263 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 order is passed without making inquiries or verification, which, should have been made;
- The order is passed allowing any relief without inquiring into the claim;
- The order has not been made in accordance with any order, direction or instruction issued by the Board under section 119; or
- The order has not been passed in accordance with any decision which is prejudicial to the assessee, rendered by the jurisdictional High Court or Supreme Court in the case of the assessee or any other person.

These provisions give wide powers to Principal Commissioner. Similar changes have not been made in section 264 for orders which are prejudicial to assessee. Sections 263 and 264 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.

**Recommendations:**

- It is recommended that the earlier provisions be reinstated.
- The constitution of the authority should undergo changes, so as to effectively perform its expected role of being a mechanism for faster dispute resolution.
- Time limit for passing AAR order within 180 days from the end of month in which application is filed, should be made mandatory. Rulings of the authority should be directly appealable to the Supreme Court. For this purpose amendments in the law need to be made.

### I.1.7 Encouraging Investments into SEZ Units and Offshore Financial Centre

The incentivizing of exports continues to be important, and while there is a move with the Government to do away with the SEZ exemption all together, the Chamber would urge that this be reconsidered, and in fact some further facilitating amendments be made into the SEZ regime.

The SEZ Act, 2005 provided for MAT and DDT exemption to SEZ units and developers and accordingly, the Income-tax Act was amended to provide for the same. However, the withdrawal of the said exemption vide Finance Act 2011 has not been received well by existing units and developers who have invested substantially into SEZs based on the Government's initial promise. Further, as the service sector also contributes substantially towards the national growth, it is also important to provide the benefits to offshore financial centre.

**Suggestions:**

- To attract more industrial and infrastructural investments, it is strongly recommended that the Government should consider doing away with Minimum Alternate Tax (MAT) on SEZ to promote manufacturing, export and employment and also give it the required Infrastructure status.
- The imposition of MAT has curbed the SEZ's potential in boosting both exports and manufacturing sector besides generating jobs. The SEZ Unit to be exempted from MAT and Dividend Distribution Tax. Similar benefit can be considered for domestic manufacturing sector set up in backward zone, subject to employment creation.

### I.1.8 Direct Tax Code Bill:

The Government must accord priority and comprehensively review the DTC Bill and avoid unwanted enactments for better compliance which means rationalization and simplification of laws rather than making it cumbersome and complicated as it stands today.

The prevailing DTC system does not only target manufacturers but is also a matter of great concern for international investors who have been impacted by this aggressive approach.

**Suggestions:**

- Direct Taxes Code need to be scrapped. The govt. may consider all necessary amendments in the Income Tax Act.

### I.1.9 Retrospective Tax Law:

The retrospective law is explicitly ambiguous and degenerating to FIIs and FDIs and has led to the crowding out of foreign investments from the nation, at a time when the economy's major requirement is of foreign direct investment and financial investments.

Non-clarity over certain tax rules, especially transfer pricing and retrospective tax amendment, has led to a rise in litigations.

**Suggestions:**

- It is imperative and strongly recommended that the Government amend the law and initiate remedial changes in order to restore investor confidence and draw funds to cash sparse Indian sectors.
- The provisions attracting litigation to be made simple and assessee friendly. Multiple level appeals by the tax department, to be subjected to an independent internal judicial committee review to end continuous litigation, Decisions of tribunals and high courts to be made binding on national basis.
- To selectively consider retrospective withdrawal of retrospective amendments of the tax laws during last 5 years.
- Raids, Surveys and Searches to be limited to only very exceptional cases to be approved at the highest level.

**I.1.10 General Anti Avoidance Rules (GAAR):**

GAAR provisions will undoubtedly have far reaching implications and to ensure that the extraordinary powers are not arbitrarily exercised by officers, it is very important that the apprehensions of the taxpayers are addressed at the earliest.

Grandfathering of investments:

Rule 10U clarifies that transactions made upto August 30, 2010 will be grandfathered.

It is recommended that all investments made upto the date of introduction of GAAR should be grandfathered.

**Recommendations:**

- It is submitted that the following clarifications should be introduced:
- GAAR should apply only to abusive or highly aggressive / contrived arrangements;
- GAAR provisions should codify the substance over form doctrine;
- Tax mitigation by taking advantage of a fiscal incentive and after complying with conditions of the provision should not be covered by GAAR;
- It should be clarified that all investments made upto March 31, 2017, including income from the investments made (either earned or accrued or received before March 31, 2017 or any time later) should be grandfathered.
- Implement prospective tax laws amendment and clarity on General Anti Avoidance Rules (GAAR).
- To delete the provisions of GAAR, as it may promote unnecessary harassment and corruption

**I.1.10 (a) GAAR vs. SAAR:**

It had been stated by the FM that in a case where GAAR and SAAR are both in force, only one of them will apply to a given case and guidelines will be made regarding the applicability of one or the other. However, no clarity is brought on this regards.

**Recommendations:**
GAAR should be considered as a last resort. It should not be invoked in a case where there is compliance with SAAR and the subject matter is dealt with through a SAAR. It is only in cases of exceptionally abusive arrangements that GAAR should be invoked.

It is also recommended that the specified description of the transactions/examples to which GAAR could be applied, should be clearly laid down to restrict the wide application of this provision by the tax authorities.

**I.1.11 Non-Adversarial Tax Regime:**

The Government should do away with the regime of criminal and raid proceedings in every case in the taxation arena i.e. Income Tax, Excise, Customs Act and the Companies Act 2013, which not only deters conduct of business but also de-motivates investors. Such system also does not exist in progressive countries.

Government should amend all provisions of Criminality, Raids and Prosecution in every act/clause, which adversely impacts the growth of business since the Government's intention is to collect revenue and not to prosecute the entrepreneur. Such acts should only be imposed on willful and habitual defaulters rather than making it a general practice.

The Government should make amends to move away from this antagonistic approach and introduce a tax environment that is investor friendly, conducive and fair.

**Key Priority Areas**
- Implement Goods & Service Tax (GST)
- Reduce the number of taxes and the ambiguity/discretionary nature of taxes, especially in transfer pricing cases
- Efficient, effective and time-bound taxation related dispute resolution
- Ensure taxation does not hinder free flow of goods
- Implement independent grievance redressal cell
- Operational reforms required to get the tax base right
- Administration reforms required for consistency and increased efficiency in approach to taxation.