JMP Advisors

India Budget 2018-19

Indian Economy – marching ahead…

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1 February 2018

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Foreword

All eyes were set on the Finance Minister's briefcase as he unveiled Budget 2018-19, since it is the last full budget of this Government prior to the Lok Sabha elections due in 2019 and the first budget post the implementation of the landmark Goods and Services Tax ('GST') regime.

The Financial Year ('FY') 2017-18 has been an action-packed year marked by various noteworthy events such as India's leap by 30 spots in the World Bank's Ease of Doing Business Report in 2017 to be positioned at 100 among 190 countries, the operation of the Insolvency and Bankruptcy Code, 2016 ('IBC') in full swing, increased accountability on account of implementation of the Real Estate Regulation and Development Act, 2016 ('RERA'), markedly increased momentum in the capital markets and liberalisation of the Foreign Direct Investment policy. The historic moment, however, was the roll out of GST where the indirect taxes regime was rejuvenated with a single unified tax replacing myriad Central and State levies.

On the economic front as well, there were several changes. Following a lacklustre performance in the first half of the FY, businesses appear to be recovering and the uncertainty surrounding the introduction of GST is gradually dissipating. As a result, the economy is on a recovery trail.

Moody's have upgraded India's sovereign rating from the lowest investment grade of Baa3 to Baa2 and have revised the outlook from stable to positive, which is the first upgrade for India in 14 years. Further, as per IMF reports, India is expected to grow at 7.4% of its Gross Domestic Product (‘GDP’) as against China’s growth of 6.8% in 2018. India is therefore, well on track to cross France and Britain to emerge as the fifth largest economy after Germany by 2018. Although there has been a fiscal deficit slippage to 3.5%, the FM has announced a fiscal deficit target of 3.3% for FY 2018-19. Amendments have been proposed in the Fiscal Responsibility and Budget Management Act, 2003 to take into consideration the revised fiscal deficit target for FY 2018-19 as well as to adopt the Debt Rule and to bring down the debt to GDP ratio to 40% over time.

Budget 2018 focuses on the less privileged sectors of society and is centred around the rural, agriculture, health and infrastructure sectors, quality of education and employment generation. The Government has gone one step further from ‘Ease of doing business’ and introduced various reforms to improve ‘Ease of living’.

On the direct tax front, individuals as well as corporates may have been a tad disappointed at the slight increase in the effective tax rate. The Budget also does not seem to have taken cognizance of the recent reductions in tax rates in the U.S.

However, at the same time, there were no surprises in the fine print. A big ticket announcement is the proposal to tax Long Term Capital Gains (‘LTCG’) exceeding INR 100,000 on listed equities and equity mutual funds for all taxpayers, including Foreign Institutional Investors (‘FIIs’). The levy of Securities Transaction Tax (‘STT’), however, remains unchanged. While high net worth individuals would be disappointed with the levy of tax on LTCG, they would be relieved that Inheritance tax has not been introduced. Another key proposal is the amendment to the definition of Business Connection in line with the OECD Base Erosion and Profit Shifting (‘BEPS’) recommendations.

On the indirect taxes front, GST had stolen the thunder earlier this year and no major amendments were proposed in the other indirect taxes. The FM incentivised domestic manufacturing in certain sectors and consequently, proposed increases in customs duties on several goods to promote ‘Make in India’.

The budget, in summary, seems to have achieved a fine balance between populist measures and maintaining fiscal discipline.

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1 February 2018

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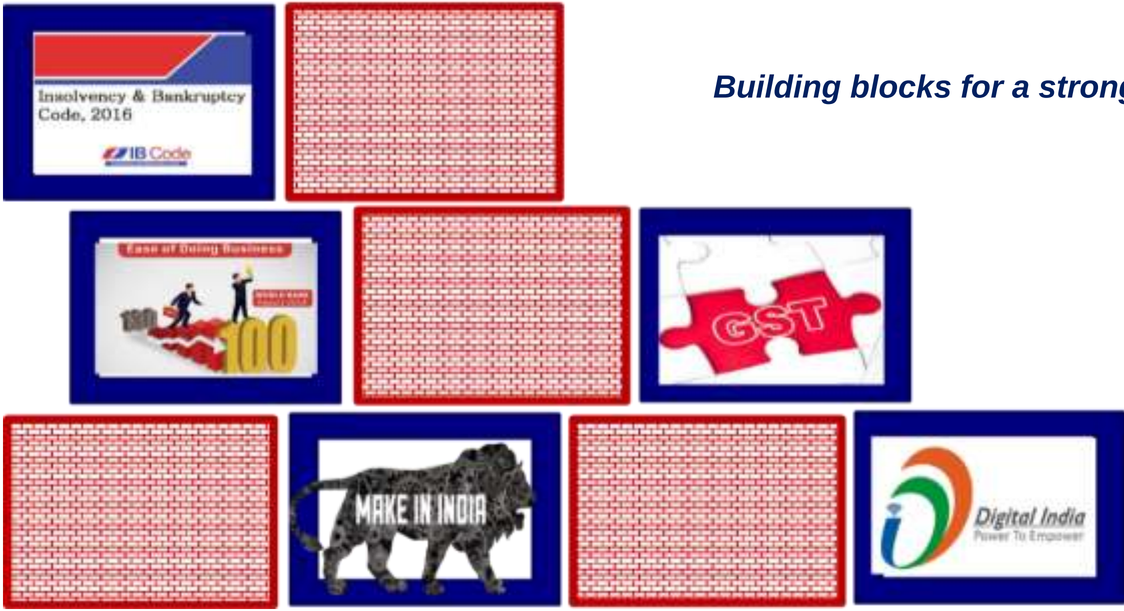
Key policy announcements



Building blocks for a stronger India

Key policy announcements

1. **Agriculture and allied sectors**

    i. It is proposed to launch ‘Operation Greens’, a mission to cater to the needs of consumers and potentially resolve seasonal and regional production of perishable commodities to promote the Farmer Producers Organizations. It is proposed to allocate INR 5 billion (~USD 80 million) for this purpose.

    ii. A ‘National Bamboo Mission’ will be launched with an outlay of INR 13 billion (~USD 200 million).

    iii. A Minimum Support Price (‘MSP’) of at least 1.5 times of the production cost is proposed to be introduced for kharif crops.

    iv. A Fisheries and Aquaculture Infrastructure Development Fund and an Animal Husbandry Infrastructure Development Fund will be set up for financing infrastructure requirements of the fisheries sector and animal husbandry sector respectively.

2. **Health**

    i. A flagship National Health Protection Scheme will be launched for over 100 million poor and vulnerable families wherein 500 million beneficiaries are estimated to be covered. The coverage per family per year for secondary and tertiary care hospitalization would be upto INR 500,000 (~USD 7,700).

ii. It is proposed to set up 24 new Government medical colleges and hospitals to ensure that there is at least 1 medical college for every 3 Parliamentary constituencies and at least 1 medical college in each state.

3. Women and poor households

i. Free LPG connections will be provided to 80 miilion poor women under the Prime Minister's Ujjwala Scheme.

ii. Electricity connections will be provided to 40 million poor households free of charge under the Prime Minister's Saubhagya Yojana.

iii. Contribution by new women employees to the Employees' Provident Fund is proposed to be reduced from 12% to 8% of wages for three years.

4. Education and employment generation

i. Measures will be taken to improve the quality of education as well as to train teachers, with the use of technology and to move from the 'black board' to the 'digital board'.

ii. A scheme will be launched named 'Prime Minister's Research Fellows Scheme' wherein 1,000 best B.Tech students from premier institutions will be selected each year to provide them facilities to undertake Ph.D in IITs and IISc, with a handsome fellowship.

iii. A National Apprenticeship Scheme is proposed to be launched to provide training to 5 million youth by 2020.

iv. In order to encourage employment generation, it is proposed that the Government will contribute 8.33%/12% of wages to the Employees' Provident Fund ('EPF') for 3 years in respect of new employees.

5. Medium, Small and Micro Enterprises ('MSME')

i. It is proposed to review the refinancing policy and eligibility criteria set by MUDRA, for better refinancing of Non-Banking Financial Companies.

ii. It is proposed to use Fintech in the financing space to help the MSME sector grow faster. Further, the income tax rate is proposed to be reduced to 25% (from 30%) for certain companies.

iii. Venture Capital Funds and angel investors need special attention for development and growth. Government has committed that more measures will be taken in this regard apart from the tax framework and Start Up India initiative.

6. Infrastructure

i. Under the Smart Cities Mission, 99 cities have been selected and these cities have started implementing various projects like Smart Roads, Solar Rooftops, Intelligent Transport Systems, Smart Parks, etc.

ii. To raise equity, National Highways Authority of India will organize its road assets into SPVs and use innovative structures like Toll, Operate and Transfer ('TOT') and Infrastructure Investment Funds ('InvITs').

iii. Capital expenditure of INR 1,500 billion (~ USD 23 billion) is proposed to be made in railways in 2018-19.

iv. The transport systems in Mumbai and Bengaluru are being expanded with a total outlay of INR 280 billion (~ USD 4 billion).

7. Financial services/Capital markets

i. A unified authority will be established for regulating all financial services in International Financial Services Centres ('IFSC') in India.

ii. The Bank recapitalization program has been launched wherein bonds of INR 800 billion (~USD 12 billion) have been issued. This will pave the way for PSU banks to lend additional credit estimated at INR 5,000 billion (~USD 77 billion).

iii. A separate policy will be introduced for hybrid instruments to attract foreign investments, especially for start-ups and venture capital firms.

iv. To give a push to the bond market, the Securities and Exchange Board of India ('SEBI') will consider mandating corporates (beginning with large corporates) to meet about 25% of their financing needs from the bond market. Further, necessary actions will be taken to permit corporate bonds with an A grade rating as eligible for investment, instead of AA grade rating.

v. Measures will be taken to eliminate the use of crypto-assets as part of the payment system.

vi. Disinvestment target for FY 2018-19 is estimated at INR 800 billion (~ USD 12 billion).

vii. Three public sector general insurance companies National Insurance Company Ltd, United India Assurance Company Ltd and Oriental India Insurance Company Ltd will be merged into a single insurance entity and will be subsequently listed.

viii. The Pradhan Mantri Vaya Vandana Yojana, under which an assured return of 8% is given by the Life Insurance Corporation of India, is proposed to be extended upto March 2020. Further, the limit for investment by senior citizens will be enhanced from INR 750,000 (~ USD 12,000) to INR 1.5 million (~ USD 24,000).

8. Technology

i. It is proposed that Niti Aayog will initiate a national program to channelize efforts in the area of Artificial Intelligence.

ii. The Department of Science & Technology will launch a Mission on Cyber Physical Systems. The allocation on Digital India programme is doubled and pegged at INR 30 billion (~USD 460 million).

iii. It is proposed to launch a scheme wherein each enterprise will be assigned a unique ID.

Key tax proposals

Direct tax

This section summarises the significant direct tax proposals announced in Budget 2018-19. These proposals are subject to enactment of the Finance Bill, 2018. Further, the direct tax proposals in the Finance Bill, 2018 are effective from FY 2018-19 unless otherwise specifically stated. References to sections are to sections in the Income-tax Act, 1961 ('the IT Act') unless otherwise stated.

I. Tax rates

1. Health and Education Cess

It is proposed that 'Education Cess on income-tax' and 'Secondary and Higher Education Cess on income-tax' shall be discontinued. A new cess, by the name of 'Health and Education Cess' shall be levied at 4% of income tax including surcharge, wherever applicable.

2. Domestic companies

It is proposed that the basic rate of income tax for domestic companies shall be 25% if the turnover or gross receipts in FY 2016-17 does not exceed INR 2.5 billion (~USD 0.04 billion) and in all other cases, the rate of income-tax shall be 30%.

3. **The maximum tax rates proposed for FY 2018-19 for the following taxpayers are as under:**

Taxpayer	Maximum marginal rate (%)
Individual/HUF/AOP/BOI	35.88
Partnership firm/LLP	34.94
Domestic company with turnover ≤ 2.5 billion in FY 2016-17	29.12
Domestic company with turnover > 2.5 billion in FY 2016-17	34.94
Foreign company	43.68

II. Provisions relating to non-residents

1. Widening the ambit of ‘Business Connection’ *[Section 9(1)(i)]*

i. The term Business Connection used in the IT Act is defined on the lines of Dependent Agent Permanent Establishment (‘DAPE’) in the Double Tax Avoidance Agreements (‘DTAAs’).

ii. The OECD BEPS Actions contain recommendations to revise the definition of Permanent Establishment (‘PE’) in the DTAAs. Pursuant to signing of the Multilateral Instrument (‘MLI’), the DAPE provisions in the DTAAs will stand modified and will have a wider scope than that of Business Connection.

iii. With a view to align the definition of Business Connection with that of PE in the DTAAs and to target commissionaire arrangements, it is proposed to amend the definition of Business Connection to include persons who habitually conclude contracts or play the principal role leading to conclusion of contracts by the non-resident, including for the transfer of ownership of, or granting the right to use, property owned by the non-resident or which the non-resident has the right to use or for provision of services by the non-resident.

iv. A second amendment is proposed to the definition of Business Connection to capture increasing use of information technology and digital media in business models, which no longer require physical presence in India. It is proposed to clarify that 'Significant Economic Presence' of a non-resident would constitute a 'Business Connection'.

v. A Significant Economic Presence would mean transactions in respect of any goods, services or property carried out by a non-resident in India, including providing downloading of data or software in India, if the aggregate payments from such transactions exceed a specific threshold, which will be subsequently prescribed. Further, it would also include systematic and continuous soliciting of business activities or engaging in interaction with such number of users, as may be subsequently prescribed, in India through digital means. These will be applicable whether or not the non-resident has a place of business in India or renders services in India.

vi. If a Significant Economic Presence is constituted, only that part of the non-resident's income which is attributable to the transactions or activities referred to above would be taxable in India.

vii. This proposal is enacted despite the fact that work under BEPS Action 1 is still under way, and is meant to be in the nature of an enabler to facilitate negotiation for further DTAA amendments.

viii. In the Explanatory Memorandum to the Finance Bill, 2018, a reference is made to anti-fragmentation rules so as to prevent the taxpayer from resorting to fragmentation of functions which are otherwise a cohesive activity, in order to avail the benefit of exemption under Article 5(4) of DTAAs. However, these provisions are not found in the Finance Bill, 2018.

2. Measures to promote IFSC *[Sections 47 and 115JC]*

i. In order to develop an international financial services hub in India and to encourage investment in IFSC, it is proposed to exempt the transfer of the following capital assets by a non-resident, from the scope of capital gains, if these are undertaken on a recognized stock exchange located in any IFSC and if the consideration for such transactions is paid/payable in convertible foreign currency:

a. Bonds or Global Depository Receipts ('GDR')
b. Rupee denominated bonds of an Indian company
c. Derivatives

ii. Corporate entities which have units in an IFSC are subject to a reduced rate of Minimum Alternate Tax ('MAT') at 9% instead of 18.5%. This benefit is proposed to be extended to Alternate Minimum tax ('AMT') in respect of non-corporate entities located in an IFSC.

3. Non-applicability of MAT to certain foreign companies *[Section 115JB]*

i. It is proposed that the MAT provisions will not be applicable in case of a foreign company whose income is computed on presumptive basis under the provisions of sections 44B (shipping business) or 44BB (business of exploration etc. of mineral oils) or 44BBA (business of operation of aircraft) or 44BBB (business of civil construction etc. in certain turnkey power projects).

ii. The proposed amendment will be effective from 1 April 2000.

III. Provisions relating to profits and gains of business or profession

1. Taxability of compensation in relation to business or employment *[Section 28(ii)]*

i. It is proposed that any compensation received or receivable due to termination/modification of the terms and conditions of any contract relating to business, whether capital or revenue, shall be taxable as 'Profits and gains of business'.

ii. It is also proposed that any compensation received or receivable by any person in connection with the termination of his employment or the modification of the terms and conditions relating thereto, whether capital or revenue, shall be taxable as 'Income from other sources'.

2. Rationalisation of provision relating to conversion of stock-in-trade into capital asset *[Section 28(via)]*

i. It is proposed that any profits or gains arising from the conversion of stock-in-trade into a capital asset shall be chargeable to tax as business income. The Fair Market Value ('FMV') of stock-in-trade as on the date on which it is converted into a capital asset shall be the consideration.

ii. On a subsequent transfer of such capital asset, its FMV at the time of conversion will be deemed to be the Cost of Acquisition (COA') of the capital asset for the purpose of computing capital gains.

3. Amendments in relation to notified Income Computation and Disclosure Standards *[Section 145A]*

i. The Central Government has notified ten Income Computation and Disclosure Standards ('ICDS') which are applicable to all taxpayers for the purposes of computation of income chargeable to income tax under the head 'Profits and gains of business or profession' or 'Income from other sources'. However, the Delhi High Court in the case of Chamber of Tax Consultants vs Union of India [299 CTR 137] had struck down certain provisions of ICDS. It is now proposed to amend the IT Act to provide requisite legislative backing to the provisions of ICDS by proposing as under:

   a. deduction to be allowed for marked to market loss or other expected loss as computed under ICDS
   b. treat gain/loss arising on account of any change in foreign exchange rates to be treated as income/loss
   c. profits and gains arising from a construction contract or a contract for providing services to be determined on the basis of percentage of completion method

ii. It is proposed to introduce the method of accounting in the following cases in order to determine the income chargeable under the head 'Profits and gains of business or profession':

   a. Inventory shall be valued at actual cost or net realisable value, whichever is lower
   b. Purchase and sale of goods or services and of inventory shall be adjusted to include the amount of any tax, duty, cess or fees actually paid or incurred by the taxpayer to bring the goods or services to the place of its location as on the date of valuation
   c. Inventories, being securities not listed on a recognised stock exchange or listed but not quoted on a recognised stock exchange with regularity from time to time shall be valued at actual cost
   d. Inventories, being securities other than above shall be valued at cost or net realisable value, whichever is lower

iii. It is further proposed that any claim for escalation of price in a contract or export incentive shall be deemed to be the income of the financial year in which reasonable certainty of its realisation is achieved.

iv. It is also proposed that assistance in the form of subsidy, if not charged in any earlier years, shall be deemed to be the income of the financial year in which it is received.

v. The proposed amendment will be effective from 1 April 2016.

4. Income from trading in agricultural commodity derivatives *[Section 43(5)]*

i. It is proposed that income from trading in agricultural commodity derivatives which are not chargeable to Commodity Transaction Tax ('CTT') will now be considered as a non-speculative transaction. Accordingly, any loss from such transaction would be treated as a normal business loss which can be carried forward and set off as per the provisions of the IT Act.

Further, the above tax treatment will facilitate cash-futures arbitrage in commodities by treating it as a single transaction.

5. Widening the scope of accumulated profits for the purpose of deemed dividend *[Section 2(22)(d)]*

i. In order to prevent certain abusive arrangements to escape tax liability on distributed profits, it is proposed to widen the scope of the term 'accumulated profits' in case of amalgamations. All profits/losses of amalgamated companies would be increased by the accumulated profits of the amalgamating company on the date of amalgamation. Thus, the accumulated profits of an amalgamating company would augment those of the amalgamated company post amalgamation.

6. Application of Dividend Distribution Tax ('DDT') to deemed dividend *[Section 115-O]*

i. It is proposed to bring deemed dividend as referred to in section 2(22)(e) within the ambit of DDT and such deemed dividend will attract DDT at 30 % (without grossing up).

7. DDT on dividend payouts to unit holders in an equity oriented fund *[Section 115R]*

i. Where any income is distributed by a mutual fund being an equity oriented fund, the mutual fund shall be liable to pay DDT at 10% on the income distributed.

8. MAT liability *[Section 115JB]*

i. With a view to facilitate the companies seeking insolvency resolution, it is proposed to reduce the aggregate of unabsorbed depreciation and book loss brought forward for computing book profit in case of a company whose application for Corporate Insolvency Resolution Process (‘CIRP’) has been admitted by the adjudicating authority.

ii. The proposed amendment will be effective from 1 April 2017.

9. Benefit of carry forward and set off of losses *[Section 79]*

i. In order to ease the restructuring and rehabilitation of companies seeking insolvency resolution, a company taking over the business of the rehabilitating company will be allowed to carry forward and set off loss of the rehabilitated company irrespective of the fact that there is a change in shareholding exceeding 49% during the year pursuant to the resolution plan under CIRP.

ii. This benefit is applicable to companies whose resolution plan has been approved under the IBC.

iii. The proposed amendment will be effective from 1 April 2017.

10. Verification of return of income *[Section 140]*

i. In case of a company with ongoing proceedings under the IBC, the return of income will be verified by an Insolvency Professional appointed by the adjudicating authority.

11. Unaddressed CIRP issues

The Finance Bill, 2018 has not addressed the following key issues relating to the insolvency process:

i. Taxability of difference between the FMV and the COA of the assets of the rehabilitated company in the hands of the company taking over the business of the rehabilitated company.

ii. Taxability of the amount of liability waived under the CIRP for the rehabilitated company.

IV. Capital Gains

1. Rationalisation of taxability in respect of immovable property *[Sections 43CA, 50C,56]*

i. It is proposed that no adjustment to sale consideration shall be made in a case where the difference between the stamp duty value and the sale consideration does not exceed 5% of the sale consideration.

ii. The proposed amendment will mitigate the hardship faced in genuine transactions in the real estate sector.

2. Limiting scope of exemption for capital gains for investment in certain bonds *[Section 54EC]*

i. It is proposed that only the LTCG arising on transfer of land or building or both are eligible for re-investment in specified bonds at any time within a period of six months after the date of such transfer. The period of lock-in for specified bonds is proposed to be increased from three years to five years.

3. Tax neutral transfers *[Section 56(2)(x)]*

i. It is proposed that any transfer of capital assets by a wholly owned subsidiary company to its holding company, or vice versa which does not constitute a transfer under section 47 will now not attract taxability under 'Income from other sources'. The proposed amendment will further facilitate the transaction of money or property between a wholly owned subsidiary company and its holding company.

ii. Such transactions between 1 April 2017 and 31 March 2018 would be taxed under section 56(2)(x) as the section is proposed to be amended with effect from 1 April 2018.

4. Taxation of LTCG *[Sections 10(38)]*

i. It is proposed to withdraw the tax exemption of LTCG arising on transfer of equity shares in a listed company or a unit of an equity oriented mutual fund or a unit of a business trust.

ii. Notwithstanding the provisions of section 112, a new section 112A, applicable from 1 April 2018 is proposed to be inserted to tax such capital gains exceeding INR 100,000 (~ USD 1,500) at 10%.

iii. No deductions will be available to offset such LTCG.

iv. The concessional tax rate of 10% is available if-

   a. STT has been paid on acquisition and transfer of equity shares in a company; or
   b. STT has been paid on transfer of a unit of an equity oriented mutual fund or a unit of a business trust

v. The Government shall notify the transactions of acquisition of equity shares for which the aforesaid condition of payment of STT shall not be applicable.

vi. The requirement of payment of STT is not applicable on transfer of a capital asset undertaken on a recognized stock exchange located in any IFSC and where the consideration for such transfer is received/receivable in foreign currency.

vii. In case of a capital asset acquired before 1 February 2018, the COA shall be deemed to be higher of –

a. Actual COA of the asset; and
b. Lower of FMV and full value of consideration received or accruing as a result of the transfer.

viii. The FMV of a listed capital asset is to be taken at the highest price quoted on the stock exchange on 31 January 2018, while in the case of unlisted capital assets, FMV is to be taken at the net asset value on 31 January 2018.

ix. The benefit of indexation on the COA and improvement in the case of a resident and the benefit of foreign currency variation in the case of a non-resident will not be considered in computing such capital gains.

x. For the purpose of section 112A, the equity oriented mutual fund may include a fund of funds which invests a minimum of 90% of its total proceeds in the units of another fund traded on a recognized stock exchange, which in turn invests a minimum of 90% of its total proceeds in equity shares of listed domestic companies.

xi. The benefit of the basic tax exemption limit would be available to such LTCG.

5. LTCG in case of FIIs *[Section 115AD]*

i. LTCG exceeding INR 100,000 (~ USD 1,500) in the hands of FIIs on transfer of listed equity shares in a company or a unit of equity oriented mutual fund or a unit of business trust will be taxable at 10% (without availing the benefit of foreign currency variation).

ii. In case the provisions of the DTAA are more beneficial than the aforesaid provisions of the proposed Section 112A, the provisions of the DTAA will prevail.

V. Tax reliefs and incentives

1. Standard deduction on salary income *[Sections 16 and 17(2)]*

i. It is proposed to introduce a standard deduction of upto INR 40,000 (~USD 600);

ii. However, exemptions currently available for transport allowance of INR 19,200 p.a. (~USD 300) and reimbursement of medical expenses amounting to INR 15,000 p.a. (~USD 200) are proposed to be withdrawn, thereby reducing the effective benefit. Transport allowance in case of differently abled persons to continue. While the exemption for reimbursement of medical expenditure is withdrawn, the rule relating to transport allowance is expected to be amended suitably.

iii. This proposal is more beneficial to individuals who receive salary by way of pension and do not receive transport allowance or medical allowance.

2. **Enhanced deduction to senior citizens *[Section 80DDB]***

   i. It is proposed to increase the deduction for payment towards medical treatment for specified diseases to INR 100,000 (~USD 1,500) for both senior citizens as well as very senior citizens.

3. **Increased deduction available for payment of medical treatment for senior citizens *[Section 80D]***

   i. It is proposed to increase the limit of deduction for payment made towards medical expenditure by an individual/member of HUF for himself, and his family and parents/member from INR 30,000 (~USD 400) to INR 50,000 (~USD 700) if paid in respect of senior citizen.

   ii. However, for senior citizens, an option to claim medical expenses instead of medical insurance premium is also available provided there is no medical insurance in force for such senior citizen.

   iii. In case where the premium for health insurance policies is paid in lump sum, it is proposed that the deduction shall be allowed proportionate to the number of years for which health insurance cover is provided.

iv. Deduction available under section 80D post amendments is tabulated as under:

Paid by	Insurance premium (INR)	Medical expenditure (INR)	Maximum aggregate deduction (INR)
Individual - for himself and family members (other than senior citizens)	25,000	-	25,000
Individual (other than a senior citizen) - for parents	25,000	50,000 (if parents are senior citizens and have not paid insurance premium)	50,000
HUF - for member of HUF	25,000	50,000 (if members are senior citizens)	50,000
Individual who is a senior citizen	25,000	50,000	50,000

4. Deduction for start-ups *[Section 80IAC]*

i. The benefit of 100% deduction of profits for any three consecutive financial years out of seven financial years at the option of the taxpayer is extended by 2 years to companies incorporated between 1 April 2019 and 31 March 2021. The deduction is available provided the turnover in any of the seven financial years from the date of incorporation does not exceed INR 250 million (~USD 4 million).

ii. The scope of 'eligible business' in a start-up has been expanded to include any innovation, development or improvement of products or processes or services or a scalable business model with a high potential of employment generation or wealth creation.

5. Deduction in respect of hiring cost of new employees *[Section 80JJAA]*

i. The benefit of a deduction of 30% of cost incurred for employing additional employees was allowed if they were employed for a minimum 240/150 days, as applicable in the relevant financial year. Considering the fact that staffing requirement may arise at any time during the year and even if the employee is employed for less than 240/150 days, as applicable in relevant financial year but continues to remain employed for 240/150 days as applicable in the immediately succeeding year, it is proposed that the benefit of deduction will not be denied.

ii. It is proposed that the benefit of the above deduction for employees engaged in manufacturing of apparel for 150 days is now being extended to footwear and leather products.

6. Deduction in respect of interest income of senior citizens *[Section 80TTA]*

i. It is proposed to introduce a deduction upto INR 50,000 (~USD 800) in respect of interest income on deposits held with banks, co-operative societies engaged in the banking business and post offices. To avoid misuse of the provision, it is proposed that this benefit of deduction will not be available if interest income is derived by any partner of a firm or any member of an association of persons or any individual from a body of individuals.

ii. Deduction of INR 10,000 (~USD 150) available currently under section 80TTA will not be available to a senior citizen/very senior citizen who claims a deduction under proposed section 80TTB.

7. Deduction for Farm Producer Companies

i. It is proposed that profits derived from specified income of Farm Producer Companies having turnover less than INR 1000 million (~USD 15 million) will be eligible for a 100% deduction from FY 2018-19 to FY 2024-25 under proposed section 80PA.

ii. Deduction under this section to be claimed after giving effect to other deductions under the chapter VIA-C.

8. Deduction not to be allowed unless return of income is furnished *[Section 80AC]*

i. It is proposed that no deduction available under chapter VIA- C, will be allowed unless the return of income is furnished on or before the due date of filing the return of income. This will include deductions available under sections 80H to 80RRB.

ii. The proposed amendment will be effective from 1 April 2017

9. Exemption on amount received from the National Pension Scheme ('NPS') ***[Section 10(12A)]***

i. It is proposed to extend the benefit of exemption upto 40% of total amount receivable on closure or opting out of the NPS scheme to all taxpayers, since earlier it was available only in case of employees.

VI. Withholding taxes

1. Withholding obligations imposed on certain exempted entities ***[Sections 10(23C) and 11]***

i. In computing the total income of any fund/trust/institution established wholly for charitable or religious purposes, it is proposed to disallow the following payments,

a. Any payment to a resident taxpayer on which tax is required to be deducted and no tax is deducted: 30% of such payment.

b. Any payment made/provided for, aggregating to an amount exceeding INR 20,000 (~USD 300) made by any mode other account payee cheque or account payee bank draft on a single day to a single payee: 100% of such payment.

2. Tax deducted at source on Interest on bonds and deposits ***[Sections 193 and 194A]***

i. It is proposed to replace the existing 8% Savings (Taxable) Bonds, 2003 with new 7.75% Government of India Savings (Taxable) Bonds, 2018.

ii. If the interest payment does not exceed INR 10,000 (~ USD 150), then tax shall not be required to be deducted on such new bonds, which is the same as in the case of the earlier bonds.

iii. It is further proposed that no tax will be withheld on interest on deposits upto INR 50,000 (~USD 800) for senior citizens.

VII. Other key proposals

1. Country by Country Report ('CbCR') *[Section 286]*

i. The due date for filing CbCR in respect of an accounting year commencing from 1 April 2016 and onwards is proposed to be extended from the due date of filing the return of income for the relevant accounting year to 12 months from the end of the reporting accounting year.

ii. The constituent entity/alternate reporting entity having a non-resident parent shall be also required to furnish CbCR if the parent entity outside India does not have an obligation to file the report in its country. The time allowed for furnishing of CbCR to such constituent entity/alternate report entity resident in India will be upto 12 months from the end of the reporting accounting year.

iii. Reporting accounting year has been defined to mean the accounting year in respect of which the financial and operational results are required to be reflected in the report.

iv. The proposed amendment is in consonance with BEPS Action 13 and will be effective from 1 April 2016.

2. **Rationalisation of provision relating to reduced tax rate for certain domestic companies *[Section 115BA]***

   i. Income of a newly set up domestic company shall, at its option, be taxed at the rate of 25%, subject to specified conditions.

   ii. It is proposed to clarify that the benefit of the reduced rate of tax is restricted to the income from business of manufacturing, production, research or distribution; and incomes which are at present taxed at a scheduler rate will continue to be so taxed.

   iii. The proposed amendment will be effective from 1 April, 2016.

3. **Entities required to apply for Permanent Account Number ('PAN') *[Section 139A]***

   i. In order to use PAN as Unique Entity Number ('UEN') for non-individual entities, it is proposed that every person, not being an individual, entering into a financial transaction of an amount aggregating to INR 250,000 (~USD 3,800) or more in a financial year shall be required to apply to the tax authorities for allotment of PAN.

   ii. It is also proposed that any person competent to act on behalf of above such entities such as managing director, director, partner, trustee, karta, chief executive officer etc. shall also apply to the tax authorities for allotment of PAN.

4. **Rationalisation of adjustments during processing of the return of income *[Section 143(1)]***
   i. It is proposed that no adjustment in respect of addition of income appearing in Form 26AS/Form 16A/Form 16 which has not been included in computing the income shall be made in respect of any return of income for FY 2017-18 and onwards.

5. **New scheme for scrutiny proceedings *[Section 143(3A)]***

   i. It is proposed to introduce a new scheme for the purpose of scrutiny proceedings to impart greater efficiency, transparency and accountability, by eliminating the interface between the tax authorities and the taxpayer, optimal utilization of resources and introduction of team-based scrutiny.

6. **Penalty for failure to furnish statement of financial transaction or reportable account *[Section 271FA]***

   i. The penalty for failure to furnish a statement of financial transaction or reportable account is proposed to be increased from INR 100 (~USD 2) to INR 500 (~ USD 8) for each day of continuing default.

   ii. In event of failure to furnish the above mentioned statements within the period specified in the notice issued, it is proposed to increase the penalty leviable from INR 500 (~USD 15) to INR 1,000 (~USD 15) for each day of continuing default.

7. **Rationalisation of prosecution provision for failure to furnish return of income *[Section 276CC]***

   i. Currently, taxpayers who wilfully fail to furnish the return of income are punishable with imprisonment and fine.

ii. The above provision is not applicable if the amount of tax payable does not exceed INR 3,000 (~USD 50).

iii. In order to prevent abuse of the above provision by shell companies or by companies holding Benami properties, it is proposed to provide that the said exclusion shall not apply in respect of a company.

8. Rationalisation of the provisions relating to CTT *[Section 117 of Finance Act, 2013]*

i. It is proposed to amend Finance Act, 2013 to include 'options on commodity derivatives' in the definition of 'taxable commodities transaction'.

ii. The rates of proposed CTT are as under:

Taxable commodities transaction	Rate	Value	Payable by
Sale of a commodity derivative	0.01%	Traded price	Seller
Sale of an option on commodity derivative	0.05%	Option premium	Seller
Sale of an option on commodity derivative, where option is exercised	0.0001%	Settlement price	Purchaser

iii. The proposed amendment will be effective from 1 April 2017.

Indirect taxes

This section summarises some of the significant indirect tax proposals announced in Budget 2018-19. The indirect tax proposals are effective from the dates mentioned therein.

The FM has emphasised 'Make in India' in this budget and has sought to incentivise domestic manufacturing by hiking customs duties on several items and also levied a 10% surcharge thereon.

No changes have been proposed in the GST law, as expected.

VIII. Customs Duty

1. **Social welfare surcharge**

   Social welfare surcharge of 10% on customs duties across the board, in addition to 3% surcharge on duties for certain specified goods. This will have a cascading effect on the cost of imports as Integrated Goods and Services Tax ('IGST') would be levied thereon, unless the Central Goods and Services Tax ('CGST') Act is amended to exclude it from the value of goods.

   i. It is proposed to have amendments for expedited dispute resolution, timelines and to adhere to commitments under Trade Facilitation Agreements.

   ii. A name change from Central Board of Excise and Customs ('CBEC') to Central Board of Indirect Taxes and Customs ('CBIC') is proposed.

iii. It is proposed that the Concept of Customs Automated System be introduced and greater reliance be placed on electronic filing and clearance of goods.

iv. A pre-notice consultation mechanism is proposed.

v. It is proposed to have a provision for issuance of supplementary show cause notices.

vi. A specific provision is proposed for audit by the Customs authority.

vii. An Advance Ruling mechanism aligned with the GST law is proposed.

viii. An option to pay Redemption fine, to be exercised within 120 days of deemed concluded proceedings for non-prohibited goods is proposed.

ix. It is proposed to have a valuation methodology for warehoused goods which are sold to any person before clearance, for the purpose of levy of IGST and Compensatory Cess.

The key amendments in the rates of basic customs duties are as follows:

Item	Existing rate	Proposed rate
Fruit juices and vegetable juices	30%	50%
Perfumes and toiletry preparations/beauty products	10%	20%

Item	Existing rate	Proposed rate
Truck and bus radial tyres	10%	15%
CKD imports of motor vehicles, motor cars, motor cycles	10%	15%
Footwear	10%	20%
Cellular mobile phones	15%	20%
Diamonds and precious stones	2.5%	5%
Watches, clocks and their spares	10%	20%
Toys and games	10%	20%
Candles	10%	25%
Lithium batteries	10%	20%
Printed circuit board assembly of mobile phones	NIL	10%
Crude edible vegetable oils	12.5%	30%
Refined edible vegetable oils	20%	35%

IX. Excise Duty

The key amendments in the rates of basic excise duties are as follows:

Item	Existing rate (INR per litre)	Proposed rate (INR per litre)
Levy of road and infrastructure cess on motor spirit (petrol and high speed diesel)	-	8.00
Unbranded petrol	6.48	4.48
Branded petrol	7.66	5.66
Unbranded diesel	8.33	6.33
Branded diesel	10.69	8.69

Basic excise duty has been reduced by INR 2 per litre and additional excise duty by INR 6 per litre. The reduction has been offset by the levy of Road and Infrastructure cess at INR 8 per litre. Hence, the price of petrol and diesel will remain unchanged.

X. Service Tax

1. Retrospective exemptions

i. Retrospective exemptions granted with respect to Life Insurance services provided to coast guard personnel by the Naval Group Fund, services by Goods and Service Tax Network to Central Government, State Government or Union territories and government's share of profit on petroleum services by government by way of grant of license or lease to explore/mine petroleum crude or natural gas or both.

ii. Refund on Service tax paid on any of the levies above, provided application is made within 6 months from the date on which the Finance Bill, 2018 receives Presidential assent.

Abbreviations

AMT	: Alternate Minimum tax	GDR	: Global Depository Receipts
BEPS	: Base Erosion and Profit Shifting	GST	: Goods and Services Tax
CbCR	: Country by Country Report	HUF	: Hindu Undivided Family
CBEC	: Central Board of Excise and Customs	IBC	: Insolvency and Bankruptcy Code, 2016
CBIC	: Central Board of Indirect Taxes and Customs	ICDS	: Income Computation and Disclosure Standards
CGST	: Central Goods and Services Tax	IFSC	: International Financial Services Centre
CIRP	: Corporate Insolvency Resolution Process	IGST	: Integrated Goods and Services Tax
		IISc	: Indian Institute of Science
CKD	: Completely Knocked Down	IIT	: Indian Institute of Technology
COA	: Cost of Acquisition	INR	: Indian Rupee
CTT	: Commodity Transaction Tax	InviT	: Infrastructure Investment Funds
DAPE	: Dependent Agent Permanent Establishment	IT Act	: Income-tax Act, 1961
		MAT	: Minimum Alternate Tax
DDT	: Dividend Distribution Tax	MLI	: Multilateral Instrument
DTAA	: Double Tax Avoidance Agreement	MSME	: Medium, Small and Micro Enterprise
EPF	: Employees Provident Fund	NBFC	: Non-Banking Finance Company
FIIs	: Foreign Institutional Investors	NPS	: National Pension Scheme
FM	: Finance Minister	OECD	: Organisation for Economic Co-operation and Development
FMV	: Fair Market Value		
FY	: Financial Year	PAN	: Permanent Account Number

PE	: Permanent Establishment
PSU	: Public Sector Undertaking
SEBI	: Securities and Exchange Board of India
STT	: Securities Transaction Tax
TDS	: Tax Deducted at Source
TOT	: Toll, Operate and Transfer
UEN	: Unique Entity Number
USD	: United States Dollar

Notes

About JMP Advisors

JMP Advisors is a leading professional services firm that offers advisory, tax and regulatory services. The vision of JMP Advisors is to be 'The Most Admired Professional Services Firm in India'. It aims to be the best as measured by the quality of its people and service to clients. The firm has a merit based culture and operates to the highest standards of professionalism, ethics and integrity. Jairaj (*Jai*) Purandare, the Founder Chairman has three and half decades of experience in tax and business advisory matters and is an authority on tax and regulation in India. *Jai* was Regional Managing Partner, Chairman-Tax and Country Leader-Markets & Industries of *PricewaterhouseCoopers* India. Earlier, *Jai* was Chairman of *Ernst & Young* India and Country Head of the Tax & Business Advisory practice of *Andersen* India.

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