B. Additional Resource Mobilisation

Rationalization of taxation of income by way of dividend

Under the existing provisions of clause (34) of section 10 of the Act, dividend which suffer dividend distribution tax (DDT) under section 115-O is exempt in the hands of the shareholder. Under section 115-O dividends are taxed only at the rate of fifteen percent at the time of distribution in the hands of company declaring dividends. This creates vertical inequity amongst the tax payers as those who have high dividend income are subjected to tax only at the rate of 15% whereas such income in their hands would have been chargeable to tax at the rate of 30%.

With a view to rationalise the tax treatment provided to income by way of dividend, it is proposed to amend the Income-tax Act so as to provide that any income by way of dividend in excess of Rs. 10 lakh shall be chargeable to tax in the case of an individual, Hindu undivided family (HUF) or a firm who is resident in India, at the rate of ten percent. The taxation of dividend income in excess of ten lakh rupees shall be on gross basis.

These amendments are proposed to be made effective from the 1st day of April, 2017 and shall accordingly apply in relation to assessment year 2017-18 and subsequent years.

[Clause 7 & 50]

Equalisation Levy

With the expansion of information and communication technology, the supply and procurement of digital goods and services have undergone exponential expansion everywhere, including India. The digital economy is growing at ten per cent per year, significantly faster than the global economy as a whole.

Currently in the digital domain, business may be conducted without regard to national boundaries and may dissolve the link between an income-producing activity and a specific location. From a certain perspective, business in digital domain doesn't seem to occur in any physical location but instead takes place in the nebulous world of "cyberspace." Persons carrying business in digital domain could be located anywhere in the world. Entrepreneurs across the world have been quick to evolve their business to take advantage of these changes. It has also made it possible for the businesses to conduct themselves in ways that did not exist earlier, and given rise to new business models that rely more on digital and telecommunication network, do not require physical presence, and derives substantial value from data collected and transmitted from such networks.

These new business models have created new tax challenges. The typical direct tax issues relating to e-commerce are the difficulties of characterizing the nature of payment and establishing a nexus or link between a taxable transaction, activity and a taxing jurisdiction, the difficulty of locating the transaction, activity and identifying the taxpayer for income tax purposes. The digital business fundamentally challenges physical presence-based permanent establishment rules. If permanent establishment (PE) principles are to remain effective in the new economy, the fundamental PE components developed for the old economy i.e. place of business, location, and permanency must be reconciled with the new digital reality.

The Organization for Economic Cooperation and Development (OECD) has recommended, in Base Erosion and Profit Shifting (BEPS) project under Action Plan 1, several options to tackle the direct tax challenges which include modifying the existing Permanent Establishment (PE) rule to include that where an enterprise engaged in fully de-materialized digital activities would constitute a PE if it maintained a significant digital presence in another country's economy. It further recommended a virtual fixed place of business PE in the concept of PE i,e creation of a PE when the enterprise maintains a website on a server of another enterprise located in a jurisdiction and carries on business through that website. It also recommended to impose of a final withholding tax on certain payments for digital goods or services provided by a foreign e-commerce provider or imposition of a equalisation levy on consideration for certain digital transactions received by a non-resident from a resident or from a non-resident having permanent establishment in other contracting state.

Considering the potential of new digital economy and the rapidly evolving nature of business operations it is found essential to address the challenges in terms of taxation of such digital transactions as mentioned above. In order to address these challenges, it is proposed to insert a new Chapter titled "Equalisation Levy" in the Finance Bill, to provide for an equalisation levy of 6 % of the amount of consideration for specified services received or receivable by a non-resident not having permanent establishment ('PE') in India, from a resident in India who carries out business or profession, or from a non-resident having permanent establishment in India.

Further, in order to reduce burden of small players in the digital domain, it is also provided that no such levy shall be made if the aggregate amount of consideration for specified services received or receivable by a non-resident from a person resident in India or from a non-resident having a permanent establishment in India does not exceed one lakh rupees in any previous year.

To provide certainty and to avoid interpretational issues, it is also proposed to define certain terms and expressions used therein. Further it also proposes to provide for the procedure to be adopted for collection and recovery of equalisation levy.

In order to provide for the administrative mechanism of the equalisation levy, it also proposes to provide for statutory authorities and also prescribes the duties and powers of the authorities to administer the equalisation levy. In order to ensure effective compliance, it also proposes to provide for interest; penalty and prosecution in case of defaults with sufficient safeguards.

Further, it also proposes to confer the power on the Central Government to make rules for the purposes of carrying out the provisions of this Chapter and further provides that every rule made under this Chapter shall be laid before each House of Parliament.

In order to avoid double taxation, it is proposed to provide exemption under section 10 of the Act for any income arising from providing specified services on which equalisation levy is chargeable.

In order to ensure compliance with the provisions this Chapter, it is further proposed to provide that the expenses incurred by the assessee towards specified services chargeable under this Chapter shall not be allowed as deduction in case of failure of the asseseee to deduct and deposit the equalisation levy to the credit of Central government.

This Chapter will take effect from the date appointed in the notification to be issued by the Central Government.

[Clause 7, 22, 160 to 177]

E. Measures to promote socio-economic growth

Exemption of income of Foreign company from storage and sale of crude oil stored as part of strategic reserves.

The existing provisions of section 5 of the Act provides for the scope of total income. In the case of a non-resident, the taxation of income takes place only if the income accrues or arises in India or is deemed to accrue or arise in India or is received in India. Section 9 of the Act provides for circumstances in which the income is deemed to accrue or arise in India. One of the circumstances providing for income to be deemed to accrue or arise in India is if any income is directly or indirectly derived through or from a business connection in India.

The Indian Strategic Petroleum Reserves Limited (ISPRL) is in the process of setting up underground storage facility for storage of crude oil as part of strategic reserves. The maintenance of strategic reserves is in India's national interest and ensures price stability for Indian oil companies. The filling cost of such facility entails huge financial burden. The Government has explored the possibility of meeting a substantial part of the financial burden through participation of private players including foreign national oil companies (NOCs) and multinational companies (MNCs) storing and selling crude oil from outside India. However, the storage of crude oil by NOCs/MNCs and its sale in India would create tax liability for these entities.

In order to achieve neutrality in terms of taxation to encourage the NOCs & MNCs to store their crude oil in India and to build up strategic oil reserves, it is proposed to amend the provisions of section 10 of the Act to provide that any income accruing or arising to a foreign company on account of storage of crude oil in a facility in India and sale of crude oil therefrom to any person resident in India shall not be included in the total income, if, -

I. such storage and sale by the foreign company is pursuant to an agreement or an arrangement entered into by the Central Government or approved by the Central Government; and

II. having regard to the national interest, the foreign company and the agreement or arrangement are notified by the Central Government in this behalf.

Since the storage of oil is expected to begin in the current financial year, this exemption would be available from the previous year 2015-16, i.e. assessment year 2016-17.

This amendment will take effect retrospectively from 1st April, 2016 and will accordingly apply in relation to assessment year 2016-17 and subsequent assessment years.

[Clause 7]

Tax Treatment of Gold Monetization Scheme, 2015

Under the existing provisions of section 10, interest on Gold Deposit Bonds issued under Gold Deposit Scheme, 1999 is exempt. Further, these bonds are excluded from the definition of capital asset and therefore exempt from tax on capital gains.

The Gold Monetization Scheme, 2015 has since been introduced by the Government of India. Wth a view to extend the same tax benefits to the scheme as were available to the Gold Deposit Scheme, 1999 it is proposed to amend Clause (14) of section 2, so as to exclude Deposit Certificates issued under Gold Monetisation Scheme, 2015 notified by the Central Government, from the definition of capital asset and thereby to exempt it from capital gains tax.

It is also proposed to amend clause (15) of section 10 so as to provide that the interest on Deposit Certificates issued under the Scheme, shall be exempt from income-tax.

These amendments are proposed to be made effective retrospectively from the 1st day of April, 2016 and shall accordingly apply in relation to assessment year 2016-17 and subsequent years.

[Clause 3 & 7]

G. Ease of doing Business/dispute resolution

Exemption from Dividend Distribution Tax (DDT) on distribution made by an SPV to Business Trust.

In respect of taxation of business trusts comprising of Real Estate Investment Trust (REITs) and Infrastructure Investment Trust (Invits) regulated by SEBI a specific taxation regime has been incorporated in the Act. Under this regime, the multiple taxation due to interposition of business trust is avoided. Under the SEBI regulation, these business trusts can hold the income generating asset either directly or through a Special Purpose Vehicle (SPV). The SPV can be a company or an LLP. Under SEBI Regulation, SPV is defined to mean any company or LLP in which REIT holds or proposes to hold controlling interest which is not less than fifty percent of the equity share capital or interest. The SPV should hold at least 80% of the assets in properties and not invest in other SPV. The existing tax regime provides that in case of REITs, the income by way of interest paid by SPV being a company to REIT is given pass through i.e. it is not taxed at the level of REIT but in the hands of respective investors of REIT. The rental income from directly held assets by REIT is also allowed a pass through. In respect of assets held through an SPV, if SPV is a company then the company pays normal corporate tax and thereafter when the income is distributed to the REIT being a shareholder, it suffers DDT which is paid by the SPV and thereafter the income is exempt both in the hands of REIT and also its investors. In case of Invits, there is a similar regime with only exception being that there is no pass through for Invits holding income generating assets directly as normally such large infrastructure projects are not held directly in the trust but are held through an SPV. As an incentive in the case of sponsor (the person setting up trust), capital gain arising at time of swap of its shareholding in SPV for units of business trust is deferred both under normal provisions and from applicability of MAT. Such gains get taxed only after actual sale of units.

It has been represented by the stakeholders that levy of dividend distribution tax at the level of SPV when it distributes its current income to the business trust makes the business trust structure tax inefficient and adversely impacts the rate of return for the investor. This is more so, as under SEBI regulations both the SPV and business trust are obligated to distribute 90% of their operating income to the investors, whereas in case of normal real estate company, there is no requirement of such annual distribution of dividends. It has been represented that because of the additional levy of DDT and associated tax inefficiency, these initiatives have not yet taken off.

In order to further rationalize the taxation regime for business trusts (REITs and Invits) and their investors, it is proposed to provide a special dispensation and exemption from levy of dividend distribution tax. The salient features of the proposed dispensation are: —

(a) exemption from levy of DDT in respect of distributions made by SPV to the business trust;

(b) such dividend received by the business trust and its investor shall not be taxable in the hands of trust or investors;

(c) the exemption from levy of DDT would only be in the cases where the business trust either holds 100% of the share capital of the SPV or holds all of the share capital other than that which is required to be held by any other entity as part of any direction of any Government or specific requirement of any law to this effect or which is held by Government or Government bodies; and

(d) the exemption from the levy of DDT would only be in respect of dividends paid out of current income after the date when the business trust acquires the shareholding referred in (c) above in the SPV. The dividends paid out of accumulated and current profits upto this date shall be liable for levy of DDT as and when any dividend out of these profits is distributed by the company either to the business trust or any other shareholder.

The amendment will take effect from 1st June, 2016.

[Clause 7, 55, 61 & 80]

Tax Incentives to International Financial Services Centre

Under the existing provisions of clause (38) of section 10, income by way of long term capital gains arising from equity shares or units of an equity oriented fund or business trust is exempt where securities transaction tax is paid.

With a view to incentivise the growth of International Financial Services Centres into a world class financial services hub, it is proposed to amend the section 10 so as to provide for exemption from tax on capital gains to the income arising from transaction undertaken in foreign currency on a recognised stock exchange located in an International Financial Services Centre even when securities transaction tax is not paid in respect of such transactions.

Under the existing provisions of the 115JB in case of a company, if the tax payable on the total income as computed under the Income-tax Act, is less than eighteen and one-half per cent of its book profit, such book profit shall be deemed to be the total income of the assessee and the Minimum Alternate Tax (MAT) payable by the assessee for the relevant previous year shall be eighteen and one-half per cent of such book profit.

With a view to provide a competitive tax regime to International Financial Services Centre, it is proposed to amend section 115JB so as to provide that in case of a company, being a unit located in International Financial Services Centre and deriving its income solely in convertible foreign exchange, the Minimum Alternate Tax shall be chargeable at the rate of nine per cent.

Further, it is proposed to amend section 115-O so as to provide that no tax on distributed profits shall be chargeable in respect of the total income of a company being a unit located in International Financial Services Centre, deriving income solely in convertible foreign exchange, for any assessment year on any amount declared, distributed or paid by such company, by way of dividends (whether interim or otherwise) on or after the 1st day of April, 2017 out of its current income, either in the hands of the company or the person receiving such dividend.

These amendments will take effect from 1st April, 2017 and will, accordingly, apply in relation to the assessment year 2017-18 and subsequent assessment years.

The existing provisions relating to securities transaction tax and commodities transaction tax provide for levy of tax on transactions in taxable securities and commodities respectively.

It is proposed to amend section 113A of the Finance (No.2) Act, 2004 so as to provide that the provisions of Chapter VII shall not apply to taxable securities transactions entered into by any person on a recognized stock exchange located in International Financial Services Centre where the consideration for such transaction is paid or payable in foreign currency, thereby exempting such transaction from securities transaction tax.

Further, it is proposed to insert section 132A in Chapter VII of the Finance Act, 2013 so as to provide that the provisions of chapter VII shall also not apply to taxable commodities transactions entered into by any person on a recognized association located in unit of International Financial Services Centre where the consideration for such transaction is paid or payable in foreign currency, thereby exempting such transaction from commodities transaction tax.

The above two amendments will take effect from 1st June, 2016.

[Clause 7, 53, 55, 230 & 234]

New Taxation Regime for securitisation trust and its investors

Under the existing provisions of Chapter-XII-EA of the Act consisting of sections 115TA, 115TB and 115TC, special taxation regime in respect of income of the securitisation trusts and the investors of such trusts has been provided. The regime provides that income distributed by the securitisation trust to its investors shall be subject to a levy of additional tax to be paid by the securitisation trust within 14 days of distribution of income. The distribution tax shall be paid @ 25% if the distribution is made to an individual or a Hindu undivided family (HUF) and @ 30% if the distribution is to others. Further, no distribution tax is to be levied if the distribution is made to an exempt entity. Consequent to the levy of distribution tax, the income of the investor, received from the securitisation trust, is exempt under section 10(35A) of the Act and the income of securitisation trust itself is exempt under section 10(23DA) of the Act.

It has been represented that under the current regime, the trusts set up by reconstruction companies or the securitisation companies are not covered although such trusts are also engaged in securitisation activity. These companies are established for the purposes of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act) and their activities are regulated by the Reserve Bank of India (RBI). It has been represented that the existing regime providing for final levy in the form of distribution tax is tax inefficient for the investors specially the banks and financial institutions. Disallowance of expenditure in respect of income received from securitisation trust increases the effective rate of taxation. Further, the non-resident and resident investors are unable to take benefits of their specific tax status.

In order to rationalise the tax regime for securitisation trust and its investors, and to provide tax pass through treatment, it is proposed to amend the provisions of the Act to substitute the existing special regime for securitisation trusts by a new regime having the following elements: -

(i) The new regime shall apply to securitisation trust being an SPV defined under SEBI (Public Offer and Listing of Securitised Debt Instrument) Regulations, 2008 or SPV as defined in the guidelines on securitisation of standard assets issued by RBI or being setup by a securitisation company or a reconstruction company in accordance with the SARFAESI Act;

(ii) The income of securitisation trust shall continue to be exempt. However, exemption in respect of income of investor from securitisation trust would not be available and any income from securitisation trust would be taxable in the hands of investors;

(iii) The income accrued or received from the securitisation trust shall be taxable in the hands of investor in the same manner and to the same extent as it would have happened had investor made investment directly in the underlying assets and not through the trust;

(iv) Tax deduction at source shall be effected by the securitisation trust at the rate of 25% in case of payment to resident investors which are individual or HUF and @ 30% in case of others. In case of payments to non-resident investors, the deduction shall be at rates in force;

(v) The facility for the investors to obtain low or nil deduction of tax certificate would be available; and

(vi) The trust shall provide breakup regarding nature and proportion of its income to the investors and also to the prescribed income-tax authority.

Further, it is proposed to provide that the current regime of distribution tax shall cease to apply in case of distribution made by securitisation trusts with effect from 01.06.2016.

These amendments will take effect from 1st June, 2016.

[Clause 3, 7, 57, 58, 59, 82 & 83]

Rationalisation of tax treatment of Recognised Provident Funds, Pension Funds and National Pension Scheme

Under the existing provisions of the Income-tax Act, tax treatment for the National Pension System (NPS) referred to in section 80CCD is Exempt, Exempt and Tax (EET) i.e., the monthly/periodic contributions during the pension accumulation phase are allowed as deduction from income for tax purposes; the returns generated on these contributions during the accumulation phase are also exempt from tax; however, the terminal benefits on exit or superannuation, in the form of lump sum withdrawals, are taxable in the hands of the individual subscriber or his nominee in the year of receipt of such amounts.

However, commutation of Government Pension and superannuation fund is exempt from taxation. The monthly contribution, annual accrued income, advances/ withdrawals for specific purposes and final withdrawal from the Recognised Provident Funds (RPFs) on superannuation are also accorded EEE status i.e. Exempt, Exempt, Exempt.

In order to bring greater parity in tax treatment of different types of pension plans, it is proposed to amend section 10 so as to provide that in respect of the contributions made on or after the 1st day of April, 2016 by an employee participating in a recognised provident fund and superannuation fund, up to 40 % of the accumulated balance attributable to such contributions on withdrawal shall be exempt from tax.

Under the existing provisions, any payment from an approved superannuation fund made to an employee in lieu of or in commutation of an annuity on his retirement at or after a specified age or on his becoming incapacitated prior to such retirement is exempt from tax.

It is proposed to amend the said provisions so as to provide that any payment in commutation of an annuity purchased out of contributions made on or after the 1st day of April, 2016, which exceeds forty per cent of the annuity, shall be chargeable to tax.

Under the existing provisions of section 80CCD, any payment from National Pension System Trust to an employee on account of closure or his opting out of the pension scheme is chargeable to tax.

It is proposed to provide that any payment from National Pension System Trust to an employee on account of closure or his opting out of the pension scheme referred to in Section 80CCD, to the extent it does not exceed forty percent of the total amount payable to him at the time of closure or his opting out of the scheme, shall be exempt from tax. However, the whole amount received by the nominee, on death of the assessee shall be exempt from tax.

Under section 17, perquisite includes the amount of any contribution exceeding one lakh rupees to an approved superannuation fund by the employer in the hands of the assessee.

Under the Part A of Fourth Schedule to the Income-tax Act contributions made by employer to the credit of an employee participating in a recognised provident fund, which are in excess of twelve percent of the salary of the employee, are liable to tax in the hands of the employee. However, there is no monetary limit for the contribution made by the employer though there is a monetary ceiling for employee’s contribution.

The limit of contribution by the employee eligible under section 80C of the Act has been increased from one lakh rupees to one lakh and fifty thousand rupees vide Finance Act(No.2), 2014. Therefore, in order to bring parity in the monetary limit for contribution by the employer and the employee, it is proposed to amend the said section and said schedule so as to provide the limit of employer’s contribution to one lakh and fifty thousand rupees, without attracting tax.

Further with a view to bring all the pension plans under one umberalla, it is also proposed to amend:-

(i) the said schedule so as to provide exemption to one-time portability from a recognised provident fund to National Pension System;

(ii) clause (13) of section 10 so as to provide that any payment from an approved superannuation fund by way of transfer to the account of the employee under NPS referred to in section 80CCD and notified by the Central Government shall be exempt from tax.

These amendments are proposed to be made effective from the 1st day of April, 2017 and shall accordingly apply in relation to assessment year 2017-18 and subsequent years.

[Clause 7, 9, 36 & 112]