BUDGET 2013

AN INSIGHT INTO KEY DIRECT TAX PROPOSALS

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RATES OF TAX FOR ASSESSMENT YEAR 2013-2014

The Finance Minister did not revise the slab rates applicable to Individuals and proposed to continue the same in the ensuing Assessment Year. The rates of tax applicable to other persons i.e. firms, co-operative societies, local authorities, domestic and foreign companies also remain the same.

Increase in the rate of surcharge:

However, the concept of taxing the "Super-rich", as vouched by Mr Aziz Premji, by way of levying additional surcharge was introduced. Following is the proposed additional burden by way of increase in surcharge:

For individuals:

Income	Prior to Finance Bill, 2013	Proposed in Finance Bill, 2013
Above Rs 1 crore	-	10%

For firms:

Income	Prior to Finance Bill, 2013	Proposed in Finance Bill, 2013
Above Rs 1 crore	-	10%

For domestic companies:

Income	Prior to Finance Bill, 2013	Proposed in Finance Bill, 2013
Above Rs 1 crore (Upto Rs 10 crores)	5%	5%
Above Rs 10 crores	5%	10%

For foreign companies:

Income	Prior to Finance Bill, 2013	Proposed in Finance Bill, 2013
Above Rs 1 crore (Upto Rs 10 crores)	2%	2%
Above Rs 10 crores	2%	5%

As a consequence of the additional surcharge, TDS provisions are also amended accordingly. Payment to a non-resident individual shall be subject to 10% surcharge in the event of payment of income above Rs 1 crore and in case of payment to a foreign company, amount of TDS shall be increased by 2% (for payment in excess of Rs 1 crore upto Rs 10 crores) and 5% (for payment in excess of Rs 10 crores).

TAXATION OF ROYALTY AND FEES FOR TECHNICAL SERVICES (FTS)

Section 115A of the Act is now amended increasing the rate of tax applicable on income in the nature of royalty and FTS of a non-resident tax payer from 10% to 25%. Accordingly, in a scenario where the non-resident is a resident of a country with whom Government of India has not entered into a tax treaty, higher tax rate of 25% shall be applicable.

As a consequence of the increase in the tax rate in section 115A, TDS rate specified under Part II of the First Schedule is amended to consider the revised rate of 25%.

DEDUCTION OF TAX AT SOURCE ON TRANSFER OF IMMOVABLE PROPERTY

Finance Bill, 2012 contained a provision for levying TDS on transfer of immovable property which was later on withdrawn while passing the Act. However, the Finance Minister has reincarnated the same by proposing to insert section 194-IA for levy of TDS on transfer of immovable property.

- ✓ Rate of TDS applicable on transfer of immovable property shall be 1%
- ✓ The same shall be applicable on the amount of sale consideration and not capital gains
- ✓ It shall be applicable on the transactions entered after 1 June 2013
- ✓ Threshold limit of transactions above which TDS is applicable prescribed is Rs 50 lacs

The fallout of the reincarnation is that TDS shall be levied on the entire amount of sale consideration rather than capital gains, thereby increasing tax burden in respect of sale of properties which are purchased several years back.

APPLICABILITY OF STAMP DUTY VALUATION ON LAND & BUILDINGS HELD AS STOCK-IN-TRADE

Prior to Finance Bill, 2013, any transfer of capital asset being an immovable property i.e. land & buildings were subject to the provisions of section 50C. As per the said section, where an immovable property is transferred for a consideration which is less than the stamp duty value, then such stamp duty value is adopted as full value of consideration. The same applied only in relation to capital assets and not to stock-in-trade.

Builders and developers cognizant to such a loophole used to transfer the properties held as stock-in-trade below the stamp duty valuation. In order to plug this loophole and override certain favourable judicial precedents[1], Finance Minister introduced a new section – 43CA.

- ✓ If the consideration for transfer of land & building (not being in the nature of a capital asset) is less than the stamp duty value, such stamp duty value shall be considered as full value consideration
- ✓ It shall be taxed under the head "Income from Business & Profession"
- ✓ Where the date of agreement and date of registration of transfer is different, stamp duty value to be considered on the date of agreement

[1] CIT v. M/S Kan Construction And Colonizers (P) Ltd [2012] 20 taxmann.com 381 (Allahabad)

INADEQUATE CONSIDERATION ON TRANSFER OF IMMOVABLE PROPERTY

Under the existing provisions of section 56(2)(vii), where there is a transfer of immovable property without consideration, stamp duty value (exceeding Rs 50,000) would be charged to tax in the hands of the recipient of the immovable property. The provisions did not cover a scenario where the immovable property is transferred for a consideration less than the stamp duty value.

In order to plug this loophole, section 56(2)(vii) is proposed to be amended to tax the differential amount (i.e. stamp duty value less agreed value) in the hands of the recipient of the property.

The said amendment may lead to double taxation i.e. in the hands of the seller under section 50C/ 43CA and in the hands of recipient under section 56(2)(vii).

TAXABILITY ON BUY-BACK SHIFTED TO COMPANIES

Prior to Finance Bill, 2013, taxability on buy back of shares by unlisted companies was governed by provisions of section 46A whereby the consideration received by shareholder on buy-back was charged to tax as capital gains.

Buy-back of shares was used as a tool for tax planning. Several companies in order to save dividend distribution tax under section 115-O opted to use the route of buy back of shares for distribution of reserves. The shareholders are either subject to lower tax rate or NIL tax on account of long term capital gains.

Taking a cue from the AAR ruling in the case of OTIS Elevators[2], wherein it was held that buyback of shares is a colourable device and that in substance it is dividend distribution, the Finance Minister has introduced a new section 115QA to treat the buy-back of shares by unlisted companies as "dividend distribution".

- ✓ Excess of buy-back consideration over the sum received on issue of shares would be taxable in the hands of the company
- ✓ Tax rate proposed is 20%
- ✓ Only unlisted companies covered
- ✓ Income arising as a result of buy-back in the hands of shareholder is exempt under section 10(35A)

TAX RESIDENCY CERTIFICATE FOR TREATY BENEFITS

Finance Act, 2012 had introduced section 90(4) which provided that a non-resident assessee in order to claim benefits under the double taxation avoidance agreement was required to obtain a Tax Residency Certificate ('TRC') from the country in which it was a Resident. A format of TRC was prescribed later on vide notification dated 17.09.2012.

However, the Memorandum to the Finance Bill, 2013 proposes that a TRC shall be necessary but not a sufficient condition to entitle the non-resident to treaty benefits and such position shall be applicable retrospectively from AY 2013-2014.

In the past, Courts[3] have accepted TRC to be sufficient in order to claim the treaty benefits.

[2] A Mauritus, In re [2012] 20 taxmann.com 52 (AAR - New Delhi)
[3] UOI v Azadi Bachao Andolan [2003 132 Taxman 373 (SC)], E-Trade Mauritius [[2010] 190 Taxman 232 (AAR]

The amendment appears ambiguous in the absence of any specific parameters other than a TRC specified under the provisions of the Act in order to claim treaty benefits.

INVESTMENT ALLOWANCE ON PLANT & MACHINERY FOR MANUFACTURING SECTOR

In order to encourage the manufacturing sector, an investment allowance is proposed by way of insertion of new section 32AC:

- ✓ A company engaged in manufacture of any article or thing is eligible for the investment allowance of 15% of the fresh investment in plant & machinery within 01-04-13 to 31-03-15
- ✓ Cost of such plant & machinery should exceed Rs 100 crores during FY 2013-14.
- ✓ Such plant & machinery should be ready to use by financial year ending 31 March 2014
- ✓ The plant & Machinery should not be installed in office premises
- ✓ Computers, computer software, vehicles, office equipments to be excluded from plant & machinery
- ✓ For AY 2015-16, allowance shall be on the additional cost of plant & machinery installed.
- ✓ Such plant & machinery installed should not be transferred within a period of 5 years (except in the case of amalgamation or demerger)

Though the investment allowance provides impetus to the manufacturing sector, excluding factory buildings from its purview and installing plant & machinery by FY 2013-14 may seem to be non-pragmatic.

EXTENSION OF SUNSET CLAUSE FOR POWER GENERATING UNITS

Section 80-IA(4) of the Act provides for deduction of profits of undertakings engaged in generation and distribution of power.

Finance Bill, 2013 seeks to extend the 'eligible date' for projects in the power sector from 31-03-2013 to 31-03-2014.

EXTENSION OF CONCESSIONAL TAX RATE ON DIVIDENDS RECEIVED FROM FOREIGN COMPANIES

Section 115BBD was inserted vide Finance Act, 2011 whereby dividends received from Foreign companies is taxable at the rate of 15% instead of maximum marginal rate of 30%. Finance Bill, 2013 proposes to extend the said benefit for one more year i.e. till AY 2014-2015.

REMOVAL OF CASCADING EFFECT OF DIVIDEND DISTRIBUTION TAX ('DDT')

Finance Act, 2012 removed the cascading effect of payment of DDT. It provided that in case any company receives, during the year, any dividend from any subsidiary and such subsidiary has paid DDT, then, dividend distributed by the holding company in the same year, to that extent, shall not be subject to DDT under section 115-O of the Act.

Finance Bill, 2013 proposes:

- ✓ Dividend received from foreign subsidiary of Indian parent to be covered
- ✓ Where dividend received from foreign subsidiary is taxed under section 115BBD, the same should be reduced while paying DDT.

TAXATION OF SECURITISATION TRUSTS

A new Chapter XII-EA proposed to be inserted to provide exemption to income of a securitization trust from the activity of securitization.

'Specified purpose distinct entity' regulated under the SEBI (Public Offer and listing of Securitized Debt Instruments) Regulations, 2008 and 'Special Purpose Vehicles' regulated by the guidelines on securitsation of standard assets issued by the RBI, to qualify for the exemption

Distributions by the specified securitization trusts to be liable to additional income-tax at the following rates:

- ✓ 25% in case of income distributed to individuals and HUF
- ✓ 30% in case of income distributed to others
- ✓ No additional income-tax to be payable in respect of any income distributed to any person whose income is not chargeable to tax under the Act

DEFERMENT OF GAAR

The Expert - Shome Committee had recommended deferment of the provisions of General Anti-Avoidance Rule (GAAR) to be implemented with effect from FY 2016-17. Instead of deferring GAAR by 3 years as recommended by the Committee, GAAR applicability is now proposed to be deferred by 2 years i.e. with effect from 1 April 2015.

OTHER HIGHLIGHTS

INTRODUCTION OF COMMODITIES TRANSACTION TAX

- ✓ Commodities Transaction Tax (CTT) is proposed to be levied on taxable commodities transactions viz commodity derivatives other than agricultural commodities entered into in a recognised association
- ✓ Rate of CTT proposed is 0.01% payable by the seller
- ✓ Section 36 to be amended to provide for deduction of CTT from the income from commodity transactions which are chargeable under the head "Income from Business & Profession"

LOWER SECURITIES TRANSACTION TAX ('STT')

The rates of STT[4] have been reduced on equity oriented mutual funds and futures.

[4]

Nature	Payable by	Current Rate (%)	Proposed rate (%)
Delivery based purchase of equity oriented fund	Purchaser	0.1	-
Delivery based sale of equity oriented fund	Seller	0.1	0.001
Sale of futures in securities	Seller	0.017	0.01
Sale of unit of equity oriented fund to the mutual fund	Seller	0.25	0.001

TAX REBATE

Tax rebate of Rs 2,000 for resident individuals with total income up to Rs 500,000 has been proposed by amending section 87 of the Act.

EXEMPTION TO VENTURE CAPITAL FUNDS ('VCF')

Under the existing provisions, an exemption is available for income earned by SEBI registered VCF and VCC from investment made in VCU as defined in Section 10(23FB) of the Act.

It is proposed that income earned by companies and trust registered as VCF under the AIF Regulations under sub category of Category I AIF of SEBI to be exempt, subject to fulfilment of certain conditions.

EXEMPTION TO INVESTOR PROTECTION FUND

Income earned by the Investor Protection Fund set up by the depositories in accordance with the SEBI (Depositories and Participants) Regulation, 1996 will be exempt from tax. Any such exempt income shared by such fund with a depository shall be chargeable to tax in the hands of the fund in the year in which income is shared.

INCREASE IN SUM ASSURED FOR LIFE INSURANCE POLICIES

Under the existing provisions of section 10(10D), any sum received under life insurance policy, including bonus thereon, will be exempt provided premium paid for such policy does not exceed 10% of actual capital sum assured.

It is proposed to introduce a new proviso in sub clause (d) for specifying a higher limit of 15% in cases of policies on the life of a person with severe disability.

KEYMAN INSURANCE POLICY TIGHTENED

A keyman insurance policy means the policy on the life of key employees/ directors. Expenditure on keyman insurance policy is allowable business expenditure in the hands of payer firm/ company. However, amount received on maturity was not exempt under section 10(10D).

It was noticed that keyman insurance policies were later on assigned to the keyman before its maturity such that the keyman can avail the exemption under section 10(10D). Certain judicial precedents[5] in the past have allowed the said arrangement. Accordingly, Finance Bill, 2013 provides that a keyman insurance policy which has been assigned to a person during his term with or without consideration shall be continued to be treated as keyman insurance policy for the purposes of Sec. 10(10D). Therefore, the receipt of surrendered value of keyman insurance policy would be taxable in the hands of the recipient and it will not get exemption under Section 10(10D).

DEFECTIVE RETURN

Section 139(9) provides that where the Assessing Officer considers that the return of income furnished by the assessee is defective, he may intimate the defect to the assessee and give him an opportunity to rectify the defect within a period of fifteen days.

[5] CIT vs. Rajan Nanda & Others [2012] 18 taxmann.com 98 (Delhi)

Finance Bill, 2013 proposes to amend the Explanation to section 139(9) so as to provide that the return of income shall be regarded as defective unless the self assessment tax together with interest, if any, has been paid on or before the date of furnishing of the return.

ADDITIONAL DEDUCTION OF INTEREST ON HOUSING LOANS

Interest on amounts borrowed for the purpose of acquisition/ construction of Self-occupied ('SOP') house property is allowed as a deduction to the extent of Rs 150,000 under section 24 of the Act. It is now proposes to give additional deduction of interest by introducing new section 80EE:

- ✓ Interest upto Rs 100,000 is proposed to be allowed as deduction
- ✓ The loan is sanctioned between 1 April 2013 and 31 March 2014
- ✓ The amount of loan does not exceed Rs 25 lacs
- ✓ The value of the residential property does not exceed Rs 40 lacs
- ✓ The benefit is only for first-home buyers.

TDS ON LONG TERM INFRA BONDS

Presently, a lower TDS rate of 5% applies on interest in respect of monies borrowed by an Indian Company in foreign currency or by issue of long term infrastructure bonds under section 194-LC.

It is proposed that such bonds issued by an Indian company and subscribed to by a non resident from monies deposited in foreign currency in designated account as converted in rupees will be deemed to be subscribed in foreign currency and a lower withholding rate of 5% will apply.

DIVIDEND DISTRIBUTION BY MUTUAL FUNDS

Under the existing provisions of section 115R, any amount of income distributed by the specified company or a Mutual Fund to its unit holders is chargeable to additional income-tax. In case of any distribution made by a fund other than equity oriented fund to a person who is not an individual and HUF, the rate of tax is 30% whereas in case of distribution to an individual or an HUF it is 12.5% or 25% depending on the nature of the fund.

In order to provide uniform taxation for all types of funds, other than equity oriented fund, it is proposed to increase the rate of tax on distributed income from 12.5% to 25% in all cases where distribution is made to an individual or a HUF.

Further, in order to bring parity in taxation of income from investment made by a non-resident Investor in an IDF whether set up as a IDF-NBFC or IDF-MF, it is proposed to amend section 115R to provide that tax at the rate of 5% on income distributed shall be payable in respect of income distributed by a Mutual Fund under an IDF scheme to a non-resident Investor.

ELECTRONIC FILING OF WEALTH TAX RETURNS

Certain classes of persons shall be notified, who will be required to file the return of net wealth in electronic form without enclosing annexures. The annexures will be required to be produced before the assessing officer on demand.

AMENDMENT IN DEFINITION OF CAPITAL ASSET

Under the existing definition of a capital asset under section 2(14), certain categories of properties including agricultural land have been excluded. It is proposed that a land to be called agriculture land:

- ✓ Should not be situated in an area within 2 kilometers of local limits of municipality etc., these 2 kilometers shall be measured aerially, and population of municipality etc. is more than 10,000 but not exceeding 1,00,000; or
- ✓ Such land should not be situated within 6 kilometers of the municipality having population of more than 1,00,00 but not more than 10 lacs or
- ✓ Such land should not be situated within 8 kilometers if population of municipality etc. is more than 10 lacs.

DEDUCTION FOR ADDITIONAL WAGES

Section 80JJA has been amended to restrict the deduction of 30% of additional wages paid to new workmen. The additional deduction for wages paid to new workmen employed is now proposed to be available only to Indian company deriving profits from manufacture of goods in a "factory".

Further, the same will not be allowed in case the factory is hived off, transferred from another existing entity or acquired by amalgamation.

POWERS OF OFFICER TO CONDUCT SPECIAL AUDIT EXPANDED

It is proposed that the tax authorities will be empowered to direct special audit under section 142(2A) if they find it necessary having regard to the volume of the accounts, doubts about the correctness of the accounts, multiplicity of transactions in the accounts or specialized nature of business activity of the taxpayer.

DEDUCTION FOR BAD DEBTS IN CASE OF BANKS

Under the provisions of section 36(1)(viia), in computing the taxable income of certain categories of banks, deduction towards provision for bad and doubtful debts is available as a specified percentage of the total income and of the aggregate average advances made by the rural branches. Further, deduction for bad debts written off is also available under section 36(1)(vii) read with section 36(2) to the extent that such bad debts exceed credit balance in the provision for bad and doubtful debts made.

Finance Bill, 2013 clarifies that for the purpose of claiming deduction in respect of bad debts actually written off, no distinction to be made in provision for doubtful debts in respect of rural advances and other advances.