POST-BUDGET MEMORANDUM

on

DIRECT TAX LAWS 2017-18

THE FINANCE BILL - 2017

Bombay Chartered Accountants' Society
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Mr. Arun Jaitley
Hon. Minister of Finance
Government of India
North Block
New Delhi - 110 001.

Date : 8th March 2017

Respected Sir,

THE FINANCE BILL - 2017

We compliment you for the focused and non populist Budget that was presented on 1st February. The idea of combining the Rail Budget and the Finance Budget is also a welcome one.

We also wholeheartedly support the various initiatives taken by the government in expanding the formal economy and reducing the use of cash in the daily transactions that the people of India enter into.

The Housing-for-all is truly a one of its kind social project in the world. Nobody has attempted a project of this scale in such a short time. And the budget proposals for Affordable Housing are in the right direction towards this project. We appreciate the deep thought but simple provisions to incentivize the private sector to put their might behind this project. We feel the proposals, be it the Industry status, tax holidays or interest subvention, are adequate and will attract a lot of serious players in the Affordable Housing sector.

Many of the provisions like three moving up the indexation base year, reducing the holding period for long term capital gains, deferring the incidence of tax in JDA etc will additionally achieve the task of bringing more land supply for development.

We take this opportunity to make certain suggestions for rationalization of law, rectification of certain anomalies in the proposed amendments as also clarifying certain ambiguities so that the amendments meet the intended objectives of the government.

We would be happy to personally explain the suggestions if we are presented with an opportunity to do so.

For **Bombay Chartered Accountants' Society,**

Chetan Shah
President

Ameet N. Patel
Chairman, Taxation Committee

CC:

- Shri Santosh Kumar Gangwar, Minister of State for Finance
- Shri Arjun Ram Meghwal, Minister of State for Finance
- The Finance Secretary
- Dr. Hasmukh Adhia, The Revenue Secretary, Ministry of Finance
- The Chairman, Central Board of Direct Taxes
- Joint Secretary, TPL-I
- Director, TPL-I
- Director, TPL-II

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1. **Clause 6 - Sec 10(38) - genuine cases should be protected**

We welcome the government's resolve to prevent the misuse of the exemptions provided in section 10. The misuse of section 10(38) by unscrupulous investors and market operators who work hand in glove to bypass the law and evade taxes has got to be stopped. The proposed amendment in section 10(38) is therefore, in principle, required.

However, as rightly pointed out in the Explanatory Memorandum, there is a need to protect the genuine investors who could have acquired shares without paying STT. In particular, the following types of acquisitions will not involve payment of STT:

1. Shares issued to employees under ESOP schemes.
2. Transfer amongst current and former employees of shares vested from a former ESOP scheme.
3. Investments made/shares acquired by regulated entities such as SEBI registered Alternate Investment Funds, Domestic Venture Capital Funds, and Foreign Venture Capital Investors; And also investments (of fresh issuances) of Mutual Funds, FPI Category I, II, III, or transactions in regulated entities, such as insurance companies, banks, etc.
4. Issue of fresh shares to promoters, post 1st October, 2004 / issue of equity shares in a preferential issue under the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009.
5. Inter-se transfer of equity shares within the promoter group.
6. Transactions which are specifically excluded from the definition of transfer by section 47 of the Income-tax Act, which include inheritance, conversions, etc.
7. Corporate restructuring approved by a Court/NCLT – e.g. mergers, demergers etc.
8. Issue of equity shares under the Qualified Institutions Placement ('QIP') route under the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009.
9. Equity shares received pursuant to split or consolidation of shares of a listed company.
10. Equity shares of a listed company issued pursuant to slump sale of business to such listed company.
11. Equity shares of a listed company acquired off-market pursuant to an approval obtained

from the Indian regulatory authorities.

12. Equity shares acquired pursuant to a group restructuring scheme.
13. Equity shares acquired by a subsidiary company from its parent and vice versa.
14. Equity shares issued by private limited company which is subsequently listed on stock exchange.

Further, even if STT has actually been paid at the time of acquisition of shares, practically, it would be very difficult for a shareholder to prove this. When shares are sold several years after the date of acquisition, the shareholder would have difficulty in tracing the documents evidencing the acquisition.

Suggestions:

Care must be taken to ensure that the various types of acquisitions listed above are notified for being excluded from the rigours of the amendment proposed in section 10(38).

Where the holding period of the shares exceeds 36 months, the proposed amendment should not be made applicable. In such cases, the requirement of proving that STT was paid at the time of acquisition of the shares should be removed.

2. **Clause 9(ii): Section 12A(1)(ab) –**

The time limit of 30 days provided in the new clause proposed to be inserted is too short. Many NGOs are run by volunteers. It is unfair to cast such an onerous responsibility on them. For example, where the amendment to the trust deed is sanctioned by a Court etc., it may take time to get copies of the court order. 30 days' period is impractical and merely onerous.

Suggestion:

Instead of 30 days, the time limit should be 6 months.

3. **Clause 9(ii): Section 12A(1)(ba) –**

   The condition of filing the return of income within the time specified in section 139(4A) is too harsh and unfair. There could be several genuine reasons for a charitable trust not being able to file its return in time.

Suggestion:

We therefore urge that this clause be withdrawn.

In the alternative, we suggest that there should be an enabling provision to condone the delay in case a reasonable cause is provided by the concerned trust.

4. **Clause 15 – Section 40A(3)**

   Not only in this clause, but in various other clauses (Clauses 11, 13, 16, 21, 83), there is reference to payment by "account payee cheque, account payee bank draft or use of electronic clearing system through a bank account".

   Today's fast changing technology provides several other modes of transferring money or making payments such as digital wallets, credit cards etc.

   Since the government's intention is to curb the use of cash and promote modes of payment which can be traced, it is imperative that any mode other than cash should be encouraged. It has been noticed that post the demonetisation drive, large number of people have started using digital wallets and credit cards for making payments. It is therefore necessary to bring these modes also within the list of acceptable modes of transacting.

Suggestion:

At all places where the words "account payee cheque or an account payee bank draft or use of electronic clearing system through a bank account" have been used, the following words may be added at the end - "or use of such electronic mode of payment as may be notified from time to time". This will enable the government to notify new modes of electronic transfers that may be conceptualized at a future date.

5. **Clause 22 – Section 45(5A)**

In principle, we welcome the amendment as it will bring clarity to the contentious issue of taxation of gains arising in case of Joint Development Agreements and will reduce litigation. However, there are certain anomalies in the proposals which, if removed, will make the amendment more meaningful and will cover more tax payers.

Suggestions:

a) Presently, JDAs between societies and Developers are not covered as the new section refers only to 'Individual or HUF.

We therefore suggest that the words ", being an individual or a Hindu undivided family," in the Line No. 19 of Clause 22 be deleted.

b) Presently, in the Explanation to the proposed sub section (5A), the definition of "specified agreement" refers to a registered agreement in which a person **owning** land or building or both. This is likely to cause unintended litigation and disputes.

We therefore suggest that the word "owning" in the Line No. 35 of Clause 22 be replaced with "holding".

c) Presently, Section 45(2) lays down the taxation of gains arising on conversion of a capital asset into stock in trade of a business carried on by the assessee. This provision has stood the test of time and has been well accepted by the tax payers as well as the tax department.

We therefore suggest that the proposed sub section (5A) be worded on similar lines as sub section (2) of section 45 so that there is consistency and clarity about the taxation of such transactions.

6. **Clause 26 – Section 50CA**

The proposed section will result in double taxation of the same amount in the in the hands of the payer and the receiver. Also, it is likely to create unending litigation on account of the vague and complicated definition contained in the Explanation.

Suggestion:

We therefore urge that this clause be withdrawn.

In the alternative, it is also submitted that the term 'quoted share' used in proposed section 50CA is defined as follows:

'Quoted share' means the share quoted on any recognised stock exchange with regularity from time to time, where the quotation of such share is based on current transaction made in the ordinary course of business.'

This definition is likely to create ambiguity and result in unintended litigation. The term "regularity" is highly subjective and could be with reference to the volume of transactions on the stock exchange or it could be with reference to a particular time period.

Similarly, the term "shares" is not defined. Therefore, disputes could arise as to whether preference shares are also covered by this provision.

The definition of "quoted share" may be amended as under
'Quoted share' means the equity share quoted on any recognised stock exchange and traded on not less than such number of days during the period of 12 months preceding the date of transfer as may be notified, where the quotation of such share is based on current transaction made in the ordinary course of business.'

It is also suggested that this section should be made applicable to shares of a company in which the public is not substantially interested.

7. **Clause 29 - Section 56(2)(x)**

The existing sections 56(2)(vii) and 56(2)(vii a) are being replaced by section 56(2)(x). The proposed section 56(2)(x) will have far reaching consequences. In brief, the proposal is to tax any "Person" who receives any gift in cash or kind from any other person or persons. Existing Section 56(2)(vii) only refers to gifts received by an Individual or HUF. Further, section 56(2)(viia) referred to shares received by a firm or company. By use of the word "Person" it will mean that the new section will apply to gifts received by all assessees (i.e. company, firm, LLP, Individual, HUF, AOP, BOI etc.)

The effect of this new provision will be that any amount received by following persons without consideration or for inadequate consideration will be taxable as income from other sources.

(i) Any amount settled in a private trust or any gift received by such a trust.

(ii) Any subsidy received from the Government by any company (including a public sector company) or other person.

(iii) Any bonus shares received by a shareholder from a company.

(iv) Any right shares issued to a shareholder by a company at a price below its fair market value.

(v) In the case of Buy Back of shares by a company if the shares are purchased at a price below the fair market value.

(vi) If a company, including a listed company or a firm, receives shares of a listed company without consideration or at a consideration below fair market value. (This was not taxable under section 56(2)(vii a) so far).

This suggested amendment will extinguish the entire concept of formation of private trusts in our country. At present, there is no clarity whether the status of a trust is to be determined with reference to the status of the beneficiaries or with reference to the status of the trustees. There are contradictory judicial pronouncements. In some cases the status of the trust is determined with reference to the status of beneficiaries. In other cases the trust is treated as an AOP or BOI. By use of the word "Person" in the proposed section 56(2)(x), the gift to a

private trust will be treated as gift to a "person". It is, therefore, suggested that this amendment be dropped. In the alternative, it may be provided in the Section 56(2)(x) that this section shall not apply to a trust which receives any property with a specific direction that it forms part of the corpus of the trust.

Suggestion:

We therefore suggest that the existing provisions be continued and the proposed amendment be dropped.

8. **Clause 31 - Section 71(3A) – Restriction of set off of loss from House Property**

   This proposal to restrict the set off of loss under the head "Income from House Property" to Rs. 2,00,000 per year will affect thousands of tax payers who have availed of loans in the past based on the law as it stood then. This will also adversely impact the real estate sector which is already reeling under a lot of pressure because of lack of liquidity and reduced offtake of new properties lying unsold.

   Suggestions:

   We therefore urge that this clause be withdrawn.

   In the alternative, the amendment should apply to loss arising on account of interest on loans taken after 31st March, 2017.

9. **Clause 32 – Section 79(b) r.w.Section 80(IAC):**

   a) The definition of eligible start up in 80(IAC) (4) Explanation (ii) requires that the total turnover of the business should not exceed Rs. 25 crore from 1-4-16 to 31-3-21. Clarification is required regarding turnover exceeding Rs. 25 crore in any of the previous years as any increase in a later year should not disentitle the assesse for the deduction in any earlier year.

The section as it is presently worded results in ambiguity in situations when, at a later date, the turnover of the eligible start up increases and crosses Rs. 25 crore. At that stage, the company would become ineligible for the deduction under section 80IAC. However, there are doubts about the deduction already claimed in the earlier years. Because of the ambiguity, there are chances that assessments of past years may be reopened to disallow the deduction already claimed.

Suggestion:

It cannot be the intention of the government to penalize a start up as against a company which is not a start up. As per the language of the proposed new section 79(2), a start up will never be able to carry forward any losses incurred after the period of 7 years from the date of incorporation, irrespective of whether any change of shareholding has taken place or not. Further, as a company should not be discouraged from expanding its business and increasing its turnover, the section should clearly spell out that in the event that the turnover crosses Rs. 25 crore, the start up would cease to be a start up and thus cease to be eligible for the exemption from loss of set off of losses only from subsequent years, but for the earlier years, the set off already claimed as per law would not be affected.

10. **Clause 42 - Section 92CE – Secondary Adjustments**

The proposed section is not in accordance with international best practice. Hardly any other country has such a practice. Further, the Companies Act, 2013 also does not have explicit provisions relating to 'adjustments' in the books of accounts of the assesse. In any case, Non-discrimination Article in the DTAAs could be invoked by the non-resident entities.

On another front, reciprocal secondary adjustments by the other countries may not be beneficial for India and would hurt the Government's initiative of enhancing ease of doing business in India.

Suggestions:

We therefore urge that this amendment be withdrawn.

In the alternative, we suggest that the Secondary Adjustment should not apply to resident companies covered under Domestic Transfer Pricing regulations and it should be restricted to only international transactions.

11. **Clause 43 – Section 94B - Thin Capitalisation:**

We strongly believe that this amendment is not conducive for better investment environment and is counter productive to the excellent initiatives of the government in the form of "Make in India", "Start up India" etc.

Suggestions:

We therefore urge that this amendment be withdrawn.

In the alternative, we suggest as under:

a) The provision should not apply to loss making companies;

b) Instead of simply restricting deduction on account of interest to 30% of EBIDTA, appropriate debt equity ratio should be prescribed as per international practices;

c) The terms 'Implicit or' in 1st proviso to section 94B(1) should be deleted to avoid litigation.

12. **Clause 50 - Sections 132(1) & 132(9B)**

A. 132(1) Explanation after 4th proviso and 132(1A) new Explanation - non-disclosure of reason to believe / reason to suspect

This amendment is not in line with the government's thrust on providing transparency in governance in the country. Non-disclosure of reasons is not a good practice and will give rise to unfettered powers in the hands of the tax officers. It will once again lead to a regime of tax terrorism which the present government has studiously tried to curb. Non-

disclosure of reason to believe / reason to suspect, to any person or authority or the appellate tribunal would only compel assessees to seek relief or remedy from the High Courts which in turn would lead to an increase in backlogs in the Courts. Lastly, these two amendments are proposed on a retrospective basis with effect from 1st April, 1962 and 1st October, 1975 respectively. It has been a stated intention of the government to not bring in any retrospective amendments and therefore the proposed amendment is contrary to the said intention and once gain gives rise to uncertainty in tax laws.

Suggestion:

We therefore urge that this clause be withdrawn

B. 132 (9B) - Provisional Attachment

This provision is likely to be misused and would cause harassment to tax payers. It would also lead to protracted litigation.

Suggestion:

We therefore urge that this clause be withdrawn

13. **Clause 58(i): Section 153(1):**

Suggestion:

This amendment may be supplemented by simultaneously reducing the time limit for issuing notice for selection of cases for scrutiny as provided in the Proviso to section 143(2).

14. **Clause 63 - Section 194(IB)**

We welcome this move to curb tax evasion and misuse of certain exemption sections by unscrupulous persons. However, the section as it is presently worded will cover thousands of people who may not even be paying any income-tax because their total income is below the threshold limit. Similarly, there will be thousands of tax payers in the income slab of Rs.

2,50,000 to Rs. 5,00,000 who may be impacted by this section. Practically, it would be very difficult for such persons to comply with the TDS provisions.

Suggestion:

The section should not be made applicable to those persons whose total income does not exceed Rs. 5,00,000 in the preceding financial year.

15. **Clause 75 – Section 234F**

U/s 239(2)(c), a return claiming refund can be filed within one year of the end of the assessment year. As per the proposed section 234F, even such cases would be covered and would be liable to the proposed fee. This would unnecessarily cause such persons to pay a fee even though the Revenue is not adversely affected by the late filing of the return.

Suggestion:

No fee should be charged from a person who files the return of income beyond the normal time limit and in whose case, a refund is due as per the return filed.

16. **Clause 83 - Section 269ST**

269ST(a) begins with ‘ No person shall receive an **amount …’.**

The word amount will include not only sum of money but any transfer for any value’. This is unintended and should be amended to clearly apply only to cash transactions. In fact, Memorandum brings out the intention.

Suggestion:

The word “amount” in line no. 39 in Clause 83 should be replaced with “sum of money”.

17. **Clause 86 – Section 271J:**

It is widely felt that this provision could be subjected to widespread misuse and would result in harassment of honest and genuine professionals. Also, in any case, there is no provision for preferring an appeal to the ITAT in respect of orders passed by the CIT.

> **Suggestions:**
>
> We therefore urge that this section be withdrawn.
>
> In the alternative, we suggest that the right of appeal to the ITAT be given to the affected person by way of a suitable amendment in section 253. Also, in order to provide a prospective impact of the section, an amendment should be made in the section to the effect that the section would apply to the certificates / reports issued on or after 1st April, 2017.

18. **Schedule 1 – Part III:** The lower rate of tax has been made applicable in case of smaller domestic companies whose turnover for F.Y. 2015-16 did not exceed Rs. 50 crore. This is a welcome amendment.

However, inadvertently, companies which are incorporated after 31st March, 2016 will not be entitled to the benefit of this concessional tax rate. Since the requirement of the turnover being less than Rs. 50 crore for F.Y. 2015-16 does not prohibit such an eligible company from continuing to pay tax in a later year even if its turnover crosses Rs. 50 crore, it is obvious that ultimately, the government intends to cover all companies at a later date for the reduced corporate tax rate of 25%. This was also the stated intention as per the speech made by the Honorable Finance Minister in July 2014 immediately after the present government was voted to power. That being the case, the companies incorporated after 31st March, 2016 should not be excluded from the scope of this amendment.

> **Suggestion:**
>
> The reduced rate of 25% should be made applicable to all companies incorporated on or after 1st April, 2016.

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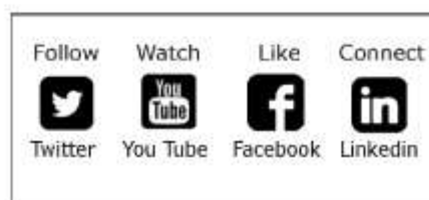

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