# PRE-BUDGET MEMORANDUM 2025

## Direct Taxes and International Taxation

**The Institute of Chartered Accountants of India**
(Set up by an Act of Parliament)
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# DIRECT TAXES
# AND
# INTERNATIONAL TAXATION

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
NEW DELHI

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# DIRECT TAXES AND INTERNATIONAL TAXATION

The Institute of Chartered Accountants of India considers it a privilege to submit this Pre-Budget Memorandum - 2025 on Direct Taxes and International Taxation to the Government. The Pre-Budget Memorandum - 2025 contains suggestions for the consideration of the Government while formulating the tax proposals for the year 2025-26.

The Memorandum contains suggestions on the policy and provisions of Income-tax Act, 1961. The suggestions have been presented Chapter-wise highlighting the relevant provision of law, the issue/concern and the suggestion. The suggestions include suggestions for rationalization of the provisions of direct tax laws, for reducing/minimizing litigation, for reducing compliance burden and for improving tax collection.

# INDEX

# 1

# HEADS OF INCOME

## 1. Section 14 - Heads of Income – Five heads of income – New head to be inserted "B. Income from shares and securities"

**Provisions of law**

Section 14 of the Act reads as follows -

14. Save as otherwise provided by this Act, all income shall, for the purposes of charge of income-tax and

computation of total income, be classified under the following heads of income :—

A.—Salaries.

B.— [***]

C.—Income from house property.

*D.*—Profits and gains of business or profession.

*E.*—Capital gains.

*F.*—Income from other sources.

**Issue**

"B- Interest on Securities" was omitted by the Finance Act, 1988 w.e.f. 1.4.1989.

Income from shares and securities by way of dividend, interest, capital gains can be classified under a separate head to simplify the scheme of taxation. This will also address the problems in classifying the income from transfer of shares and securities as capital gains and business income.

**Suggestion**

It is suggested that a new head of income "B -Income from shares and securities" be inserted and all provisions relating to taxability of income therefrom, whether by way of dividend, interest or capital gains be covered thereunder.

# 1-A

# SALARIES

## 2. Section 16(ia) – Standard Deduction from salary income – Need for regular enhancement of standard deduction on the basis of cost inflation index as per the default tax regime

### Provision of Law

Salaried employees are allowed standard deduction u/s 16(a) @ Rs. 75,000 or the amount of salary, whichever is lower, under the default tax regime u/s 115BAC(1A) to cover expenses incurred during the course of the employment.

If they opt out of the default tax regime and pay tax as per the normal provisions of the Act, then the standard deduction u/s 16(a) would be Rs.50,000 or the amount of salary, whichever is lower.

### Issue

There are various expenses that the employees incur during the course of employment which they cannot claim as deduction. At the same time, the few exemptions that are available to them u/s 10 are subject to upper limits which have been fixed several years back and virtually serve no purpose on account of inflation.

Employees during the course of their employment incur various expenses, including for upgrading skill, for rendering their services as employees, deduction for such expenses needs to be enhanced every year.

Ideally, standard deduction may be revised every year on the basis of cost inflation index i.e. standard deduction to be revised annually based on CII.

For avoiding leakage of revenue, such deduction under the default tax regime may be linked to cost inflation index just like as it happens for income under the head capital gains.

### Suggestion

It is suggested that the standard deduction u/s 16(ia) under the default tax regime under section 115BAC(1A) may be enhanced keeping in mind the rate of inflation and purchasing power of the salaried individuals. It may be linked to cost inflation index for regular enhancement in deduction amount similar to deduction available for computing long-term capital gains.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 3. Section 17(2)(vi) - Taxation of ESOP in case of employees of eligible start-ups – Request for deferral of taxability for all start ups registered with DPIIT

### Provision of Law

As per section 17(2)(vi), the value of any specified security or sweat equity shares allotted or transferred, directly or indirectly, by the employer, or former employer, free of cost or at a concessional rate to the assessee is included in the employee's salary as a perquisite.

As per section 156(2), where the income of the assessee includes income of the nature specified in section 17(2)(vi), and such specified security or sweat equity shares referred to in the said clause are allotted or transferred directly or indirectly by the current employer, being an eligible start up referred to in section 80-IAC, the tax and interest on such income included in the notice of demand under section 156(1) shall be payable within 14 days –

(i) After the expiry of 48 months from the end of the relevant assessment year; or

(ii) From the date of the sale of such specified security or sweat equity share by the assessee; or

(iii) From the date of the assessee ceasing to be the employee of the employer who allotted or transferred him such specified security or sweat equity share,

whichever is earliest.

### Issue

The deferment in collection of tax on specified security or sweat equity shares exercised by employees of 'eligible start ups' (i.e. start-ups set up on or after 1st April 2016 approved by Inter Ministerial Board of Certification as notified by the Central Government for claiming benefit under section 80-IAC) will benefit only a fraction of employees registered with The Department for Promotion of Industry and Internal Trade ('DPIIT').

The provision provides for taxation of perquisite of specified security or sweat equity shares in the year of allotment/transfer of shares whereas the collection of tax is deferred to future date, which is 14 days from the date of

a) completion of 48 months from the end of the relevant assessment year.

b) shares are sold; or

c) employee leaves the employment of the eligible start up,

whichever is earliest.

As per section 140A read with section 156, it appears that that notice of demand will be raised on the employee, but it will be enforced on a future date. Reference to payment of 'interest' by the employee in section 140A and section 156(2) leads to uncertainty with respect to the employee's liability to pay interest since there is no corresponding amendment in section 234A or 234B.

**Suggestion**

It is suggested that -

(i) Tax deferral on specified security or sweat equity shares may be extended to employees of all start-ups registered with DPIIT.

(ii) Instead of issue of demand notice followed by deferment of collection, a scheme can be enacted on similar lines as that of section 45(2) dealing with conversion of capital asset into stock-in-trade where the income is quantified in the year of conversion but the taxation is deferred till the year of sale of converted asset/completion of 48 months from the end of the relevant assessment year/on leaving employment of the eligible start up, whichever is earliest. The trigger for taxation of perquisite can itself be on the happening of any of the prescribed events.

If, however, the provision is retained in current form, consequential amendments may be made in section 234A, 234B and 220(1) to clarify that employee's liability to pay interest gets triggered only in case the employer fails to deduct tax within the prescribed deferment period.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 4. Section 17(2)(iii) – Perquisite taxable in the case of specified employees – Salary threshold of Rs.50,000 no longer relevant and may be removed

### Provision of Law

Section 17(2) contains the inclusive definition of "perquisite". Sub-clause (iii) thereof provides that the value of any benefit or amenity granted or provided free of cost or at a concessional rate, inter alia, by any employer to an employee whose income under the head "Salaries", exclusive of the value of all benefits or amenities not provided by way of monetary payment, exceeds Rs.50,000. The threshold of Rs.50,000 has been effective from 1.4.2002.

Sub-rules (2) to (6) of Rule 3 provide for valuation of perquisite specified in Section 17(2)(iii).

### Issue

Section 17(2)(iii) providing for a salary threshold of Rs.50,000 for falling within the ambit of "specified employee" is not of any relevance in the current context, after more than 22 years.

### Suggestion

It is suggested that clause (iii) of section 17(2) may be made applicable to all employees irrespective of salary threshold. The individual sub-rules (2) to (6) could provide some individual threshold above which the value of benefit would be chargeable to tax as perquisite.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 5. Section 10(12B) – Benefit of tax-free withdrawal from NPS to both employee and non-employee subscribers under section 10(12A) – Similar provision to be incorporated in section 10(12B)

### Provision of Law

Section 10(12A) provides for an exemption of upto 60% of the total amount payable to an assessee contributing to the NPS on closure of his account or on his opting out of the scheme. In cases of partial withdrawal from NPS, section 10(12B) provides for exemption of upto 25% of contributions made by an employee.

The benefit of exemption under section 10(12A) which was initially available only to employees had been extended by the Finance Act, 2018 to all assessees, in order to provide a level playing field to both employee and non-employee assessee subscribers.

### Issue

Till now, however, a similar provision has not been introduced in respect of benefit of exemption under section 10(12B), consequent to which such benefit of exemption in case of partial withdrawal continues to be restricted to employees alone.

To provide equity between the employee and non-employee subscriber, similar provision may be incorporated in section 10(12B) to extend the benefit available thereunder to non-employee subscribers.

### Suggestion

It is suggested that the amendment as made in section 10(12A) may also be made in section 10(12B) thereby extending the benefit of exemption in case of partial withdrawal to non-employee subscribers as well.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 6. Section 10(13) - Payment from approved superannuation fund - Exemption to be extended to amount received on voluntary retirement

### Provision of Law

Section 10(10AA) provides for exemption for payment received as cash equivalent of leave salary in respect of earned leave period at the time of retirement whether on superannuation or otherwise.

Section 10(13) provides for exemption with regard to payment from an approved superannuation fund. Section 10(13)(ii) provides for exemption in the hands of the employee in respect of the amount received on commutation of the annuity in case of retirement at or after a specified age or on becoming incapacitated prior to such retirement

### Issue

Section 10(13), however, does not cover commutation of an annuity paid on voluntary retirement of the employee. Section 10(10AA), as mentioned above, has taken care of such case by using the terminology "or otherwise". Since the intention of the law makers is clear by the wordings of section 10(10AA), section 10(13)(ii) may be appropriately amended to include the words "or otherwise". This will provide relief to genuine taxpayers who are taking voluntary retirement.

### Suggestion

It is suggested that section 10(13) may be amended to exempt commuted value received by an employee from the superannuation corpus standing to his credit at the time of voluntary retirement, by including the words "or otherwise" in line with section 10(10AA) of the Income-tax Act, 1961.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

# 1-B

# INCOME FROM HOUSE PROPERTY

## 7. Section 23(1) – Higher of Expected rent and actual rent is the Gross Annual Value of property - Actual rent to be chargeable to tax

### Provision of Law

### Section 23(1) reads as follows -

"For the purposes of section 22, the annual value of any property shall be deemed to be—

(a) the sum for which the property might reasonably be expected to let from year to year; or

(b) where the property or any part of the property is let and the actual rent received or receivable by the owner in respect thereof is in excess of the sum referred to in clause (a), the amount so received or receivable; or

(c) where the property or any part of the property is let and was vacant during the whole or any part of the previous year and owing to such vacancy the actual rent received or receivable by the owner in respect thereof is less than the sum referred to in clause (a), the amount so received or receivable:

*Provided* that the taxes levied by any local authority in respect of the property shall be deducted (irrespective of the previous year in which the liability to pay such taxes was incurred by the owner according to the method of accounting regularly employed by him) in determining the annual value of the property of that previous year in which such taxes are actually paid by him.

**Explanation** - For the purposes of clause (*b*) or clause (*c*) of this sub-section, the amount of actual rent received or receivable by the owner shall not include, subject to such rules as may be made in this behalf, the amount of rent which the owner cannot realise."

### Issues

In cases where expected rent is higher than actual rent, it is the expected rent which is chargeable to tax and not the actual rent, except in cases where actual rent is lower because of vacancy.

The *Explanation* to section 23(1) requires the unrealised rent to be deducted from the amount of actual rent received or receivable by the owner. However, if the expected rent is higher than the actual rent, then, the

expected rent would be the gross annual value. In such a case, unrealised rent should be deducted from the expected rent.

In effect, since, at present, the higher of the expected rent and actual rent is the gross annual value, unrealised rent should be deductible from the gross annual value. This is also the manner in which deduction for unrealised rent is provided in the return forms, an extract of which is given below -

| **Schedule HP** | | **Details Of Income From House Property** *(Please Refer Instructions) (Drop down to be provided indicating ownership of property)* | | | | |
|---|---|---|---|---|---|---|
| HOUSE PROPERTY | 1 | **Address of property 1** | **Town/ City** | **State** | **Country** | **PIN Code/ ZIP Code** |
| | | | | | | |

| | | | |
|---|---|---|---|
| **Is the property co-owned?** o Yes o No (if "YES" please enter following details) | | | |
| **Your percentage of share in the property (%)** | | | |
| **Name of Co-owner(s)** | **PAN/Aadhaar No. of Co-owner(s)** | **Percentage Share in Property** | |
| I | | | |
| II | | | |

| | | | |
|---|---|---|---|
| *[Tick* þ *the applicable option]* o Let out o Self-occupied o Deemed let out | **Name(s) of Tenant(s) (if let out)** | **PAN/ Aadhaar No. of Tenant(s) (Please see note)** | **PAN/TAN/ Aadhaar No. of Tenant(s)** (if TDS credit is claimed) |
| | I | | |
| | II | | |

| | | | | | |
|---|---|---|---|---|---|
| a | Gross rent received or receivable or lettable value | | | 1a | |
| b | The amount of rent which cannot be realized | 1b | | | |
| c | Tax paid to local authorities | 1c | | | |
| d | Total (1b + 1c) | 1d | | | |
| e | Annual value (1a – 1d) *(nil if self-occupied etc. as per section 23(2) of the Act)* | | | 1e | |
| f | Annual value of the property owned (own percentage share x 1e) | | | 1f | |
| g | 30% of 1f | 1g | | | |
| h | Interest payable on borrowed capital | 1h | | | |
| i | Total (1g + 1h) | | | 1i | |
| j | Arrears/Unrealized rent received during the year less 30% | | | 1j | |
| k | Income from house property 1 (1f – 1i + 1j) | | | 1k | |
| | (fill up details separately for each property) | | | | |
| 2 | Pass through income/loss if any * | | | 2 | |

**Suggestion**

It is suggested that the real income i.e., Actual rent received/receivable be subject to tax under the head "Income from house property" and not expected rent.

Without prejudice to the above suggestion, if expected rent is to continue, Explanation to section 23(1) may be reworded as given below –

For the purposes of this sub-section, the amount of actual rent received or receivable by the owner or the expected rent, as the case may be, shall not include, subject to such rules as may be made in this behalf, the amount of rent which the owner cannot realise.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 8. Section 23(5) – Annual value of property held as stock in trade after two years from the end of the financial year in which the certificate of completion of construction of the property is obtained will be subject to tax – Removal of this sub-section

**Provision of law**

Section 23(5) reads as follows -

*"Where the property consisting of any building or land appurtenant thereto is held as stock-in-trade and the property or any part of the property is not let during the whole or any part of the previous year, the annual value of such property or part of the property, for the period up to two years from the end of the financial year in which the certificate of completion of construction of the property is obtained from the competent authority, shall be taken to be nil."*

**Issue**

In effect, section 23(5) provides for taxability of annual value after 2 years from the end of the financial year in which certificate of completion of construction of property is obtained. This provision may cause hardship to genuine developers who are unable to dispose off their stock in the slump. In many cases, the developers pay interest on funds borrowed for construction. Further, under section 71(3A), there is a ceiling of Rs. 2 lakhs for set-off of loss from house property against any other head of income. The combined effect of application of sections 23(5) and 71(3A) poses genuine difficulty for the developers.

**Suggestion**

It is suggested that sub-section (5) of section 23 be removed.

Alternatively, without prejudice to the above,

(i) the annual value of property being held as stock in trade should be taken as Nil under section 23(5) for at least five years from end of the financial year in which certificate of completion of construction is obtained from competent authority.

(ii) section 71(3A) be amended so as to exclude its applicability to income from house property under section 23(5)

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 9. Section 27 read with Section 269UA(f) – Lessee deemed to be the owner of premises leased for a term of not less than 12 years –No deduction for lease rent paid by the lessee to the lessor against the rental income received by him from sub-lease of premises

### Provision of Law

As per section 27 read with section 269UA(f), a lessee is deemed to be the owner of the premises leased for a term of not less than 12 years. When such a lessee sub-leases the property, the income derived from the sub-lease is taxed under the head "Income from House Property, since the lessee is the deemed owner as per section 27.

However, the lease rent paid by the lessee to the lessor is not allowed as a deduction while computing income from house property.

### Issue

The deductions available under "Income from house property" are restricted to those specified in Section 24, namely, deduction@30% of annual value and interest. No deduction is allowed for the lease rental paid by the lessee. As a result of the restriction on deductions, the real income (after deducting the lease rent paid) is not taxed under this section, leading to a higher taxable income than actual earnings.

### Suggestion

It is suggested that lease rent paid by the lessee to the lessor be allowed as a deduction while computing "Income from House Property" in cases where the lessee, being the deemed owner as per section 27, sub-leases the property.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 10. Section 27 & 64(1)(iv)/(vi) – Deemed ownership and clubbing provisions– Individual transferring property to spouse without consideration or for inadequate consideration is deemed to be the owner – Clubbing provisions in respect of asset transferred to spouse and son's wife - Provisions may be removed to encourage ownership of property by women

**Provision of law**

As per section 27(i), an individual who transfers otherwise than for adequate consideration any house property to his or her spouse, not being a transfer in connection with an agreement to live apart, would be deemed to be the owner of the house property so transferred.

As per section 64(1), in computing the total income of any individual, there shall be included all such income, as arises directly or indirectly—

(iv) subject to the provisions of clause (*i*) of section 27, to the spouse of such individual from assets transferred directly or indirectly to the spouse by such individual otherwise than for adequate consideration or in connection with an agreement to live apart;

(vi) to the son's wife, of such individual, from assets transferred directly or indirectly on or after the 1st day of June, 1973, to the son's wife by such individual otherwise than for adequate consideration;

**Issue**

In many Indian households, it is common to register property in the name of the woman. Granting property ownership rights to women is a significant step toward making them self-reliant and enhancing their economic standing. Several State Governments have incentivized registration of property in the name of women, by offering reduced stamp duty rates.

However, the provision under section 27 acts as a deterrent by deeming the transferor-spouse as the owner. The provision discourages gifts or transfers of property to a spouse, except in very specific circumstances, such as:

- Transfers made to a spouse under an agreement to live apart.
- Transfers made to a minor married daughter.

This restrictive provision discourages individuals from transferring property to their spouse, thereby negating the benefits of stamp duty rebate offered by State Governments. Also, the clubbing provisions under section 64(1)(iv)/(vi) discourage transfer of assets to spouse and son's wife.

**Suggestion**

It is suggested that the restrictive deemed ownership provision under section 27 as well as the clubbing provisions under section 64(1)(iv)/(vi) be removed to encourage property ownership by women.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

# 1-C

# PROFITS AND GAINS FROM BUSINESS AND PROFESSION

## 11. Section 32(1) - Depreciation – Deduction for Depreciation computed at the rates prescribed in New Appendix I of Income-tax Rules read with Rule 5 - Suggestion to allow depreciation as per the provisions of the Companies Act, 2013 for companies & allow depreciation on proportionate basis in case of slump sale

### Provision of Law

Section 32 read with Rule 5 provides for depreciation at the rates prescribed in New Appendix I of the Income-tax Rules, 1962.

The sixth proviso to section 32(1) provides that the aggregate deduction, in respect of depreciation on buildings, machinery, plant or furniture, being tangible assets or know-how, patents, copyrights, trademarks, licenses, franchises or any other business or commercial rights of similar nature, being intangible assets allowable to the predecessor and the successor in the case of succession referred to in clause (xiii),(xiiib) and clause (xiv) of section 47 or section 170 or to the amalgamating company and the amalgamated company in the case of amalgamation, or to the de-merged company and the resulting company in the case of de-merger, as the case may be, shall not exceed in any previous year the deduction calculated at the prescribed rates as if the succession or the amalgamation or the de-merger, as the case may be, had not taken place, and such deduction shall be apportioned between the predecessor and the successor, or the amalgamating company and the amalgamated company, or the de-merged company and the resulting company, as the case may be, in the ratio of the number of days for which the assets were used by them.

### Issues

(a) The separate rates of depreciation in the Income-tax Act, 1961 were intended as an incentive for investment in plant and machinery and to give a filip to manufacturing and other essential sectors. However, now, with the general rate of depreciation for plant and machinery being 15% and the maximum rate being capped at 40%, there is no need for separate computation based on the rates prescribed under the Income-tax Act, 1961 for companies.

(b) An issue arises as to whether depreciation can be claimed on the basis of proportionate number of days by the transferor and the transferee company in case of slump sale considering the sixth proviso to section 32(1) read with section 170.

(c) As per the sixth proviso to section 32(1), the depreciation can be claimed on the basis of proportionate number of days for which the assets were used by the predecessor and the successor, or the amalgamating company and the amalgamated company, or the de-merged company and the resulting company, as the case may be.

Due to practical and administrative difficulties, there may be a time gap between holding of the asset and using the asset so transferred. To avoid genuine difficulties in such cases, instead of the words, "used by them", the words "held by them" may be substituted in the sixth proviso to section 32(1).

**Suggestion**

It is suggested that section 32 may be amended -

(i) to provide that the depreciation computed as per the Companies Act, 2013 can be allowed as deduction under the Income-tax Act, 1961 also.

(ii) to clarify the legal position as to whether depreciation can be claimed on the basis of proportionate number of days by the transferor and the transferee company in case of slump sale also, considering the sixth proviso to section 32(1) read with section 170.

(iii) in the cases of merger or demerger, to avoid genuine difficulties due to time gap between holding of the asset and using the asset transferred, instead of the words, "used by them", the words "held by them" may be substituted in the sixth proviso to section 32(1).

***(SUGGESTION FOR REDUCING/MINIMIZING LITIGATION)***

## 12. Section 37 – Disallowance of Expenditure incurred towards Corporate Social Responsibility – Need for allowance of deduction of such expenditure

### Provision of Law

*Explanation 2* to section 37(1) provides that any expenditure incurred by an assessee on the activities relating to CSR referred to in section 135 of the Companies Act, 2013 shall not be deemed to be an expenditure incurred by the assessee for the purposes of the business or profession and deduction shall not be allowed.

As per the Companies Act 2013, it is mandatory for specified companies (as per Section 135) to spend 2% of their average profits towards Corporate Social Responsibility.

### Issue

These expenses are all connected to social and charitable causes and not for any personal benefit or gain. It is, therefore, rational to allow the same as deduction under section 37. There is no bar on allowability of CSR expenditure falling under sections 30 to 36. Therefore, there is a need to revisit this provision and allow deduction to companies of CSR expenditure incurred by them under section 37 also.

### Suggestion

It is suggested that the CSR expenses listed in Schedule VII to the Companies Act, 2013, which are not specifically covered u/s 30 to 36 may be allowed u/s 37. Expenses in the nature of contributions which are allowable under any other provision of the Act (for eg. Section 80G) may be disallowed under section 37 if the assessee is claiming benefit under that section.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 13. Section 43(5) – Speculative transaction – Eligible transaction in respect of trading in shares and commodities to be excluded.

### Provision of Law

Section 43(5) defines a speculative transaction to mean a transaction in which a contract for the purchase or sale of any commodity, including stocks and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips.

The proviso to section 43(5) provides for the transactions that shall not be deemed as speculative transaction. As per clause (d) of the proviso to section 43(5), an eligible transaction of trading in derivatives carried out in a recognized stock exchange is not deemed as a speculative transaction.

Eligible transaction is a transaction carried out electronically on screen-based systems through a stock broker or sub-broker or such other intermediary registered under SEBI Act, 1992 and which is supported by a time stamped contract note issued by the stock broker or sub-broker or such other intermediary to every client indicating in the contract note the unique client identity number allotted and PAN.

### Issue

In the earlier years, when electronic trading platforms were not as robust, intraday share transactions were not time-stamped. As a result, such transactions were classified as speculative under Section 43(5). However, with the advancement of technology and the introduction of highly effective and secure online trading systems, every transaction carried out on recognised stock exchanges is now time-stamped and meticulously tracked. This evolution in the trading mechanism ensures a greater degree of transparency and accuracy.

In line with eligible transaction of trading in derivatives, intraday transactions in shares and commodities that are time-stamped and carried out on recognised stock exchanges should not be treated as speculative. Instead, they should be classified as business income or short-term capital gains, depending on the nature of the transaction.

**Suggestion**

It is suggested that clause (f) be inserted in the proviso to section 43(5) providing that an eligible transaction in respect of trading in shares and commodities carried out in a recognized stock exchange would not be deemed to be a speculative transaction.

Eligible transaction in respect of trading in shares and commodities may be defined by inserting Explanation 3 to mean a transaction carried out electronically on screen-based systems through a stock broker or sub-broker or such other intermediary registered under SEBI Act, 1992 or through a member and which is supported by a time stamped contract note issued by the stock broker or sub-broker or member or such other intermediary to every client indicating in the contract note the unique client identity number allotted and PAN.

Alternatively, the losses from such transactions may be exempted from the restrictive provisions of section 73 requiring set-off of losses of speculation business only against profits and gains from speculative business. Such losses may be permitted to be set-off like normal business losses.

***(SUGGESTION FOR RATIONALISATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 14. Section 44AB – Audit of Accounts of persons carrying on business or profession – Clauses (b) and (d) to cover "profession referred to in section 44AA(1)"

**Provision of Law**

**Section 44AB reads as follows -**

Every person,—

(a) carrying on business shall, if his total sales, turnover or gross receipts, as the case may be, in business exceed or exceeds one crore rupees in any previous year :

Provided that …

Provided further that….

(b) carrying on **profession** shall, if his gross receipts in profession exceed fifty lakh rupees in any previous year; or

(c) carrying on the business shall, if the profits and gains from the business are deemed to be the profits and gains of such person under section 44AE or section 44BB or section 44BBB, as the case may be, and he has claimed his income to be lower than the profits or gains so deemed to be the profits and gains of his business, as the case may be, in any previous year; or

(d) carrying on **profession** shall, if the profits and gains from the profession are deemed to be the profits and gains of such person under section 44ADA and he has claimed such income to be lower than the profits and gains so deemed to be the profits and gains of his profession and his income exceeds the maximum amount which is not chargeable to income-tax in any previous year; or

(e) carrying on the business shall, if the provisions of sub-section (4) of section 44AD are applicable in his case and his income exceeds the maximum amount which is not chargeable to income-tax in any previous year,

get his accounts of such previous year audited by an accountant before the specified date and furnish by that date the report of such audit in the prescribed form duly signed and verified by such accountant and setting forth such particulars as may be prescribed.

**Issue**

Section 44ADA contains presumptive income provisions for assessees engaged in a profession referred to in section 44AA(1), whose gross receipts do not exceed Rs.50 lakhs, namely, legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or any other notified profession.

It appears that the intent of clause (b) of section 44AB is to cover a person carrying on profession referred to in section 44AA(1), as the threshold gross receipt limit mentioned therein is Rs.50 lakhs. However, clause (b) mentions

person carrying on profession, without adding that the profession should be profession referred to in section 44AA(1). Other professions should be covered within the scope of clause (a).

Likewise, clause (d) should also specifically mention profession referred to in section 44AA(1), as it is in relation to assessees eligible for section 44ADA who claims lower profits.

Clauses (a) and (e) should refer to business or profession, other than a profession referred to in section 44AA(1).

**Suggestion**

It is suggested that section 44AB be amended as follows -

*Every person,—*

*(a) carrying on **business or profession, other than a profession referred to in section 44AA(1)**, shall, if his total sales, turnover or gross receipts, as the case may be, in business exceed or exceeds one crore rupees in any previous year :*

*Provided that …*

*Provided further that…..; or*

*(b) carrying on **profession referred to in section 44AA(1)** shall, if his gross receipts in profession exceed fifty lakh rupees in any previous year; or*

*(c) carrying on the business shall, if the profits and gains from the business are deemed to be the profits and gains of such person under section 44AE or section 44BB or section 44BBB, as the case may be, and he has claimed his income to be lower than the profits or gains so deemed to be the profits and gains of his business, as the case may be, in any previous year; or*

*(d) carrying on **profession referred to in section 44AA(1)** shall, if the profits and gains from the profession are deemed to be the profits and gains of such person under section 44ADA and he has claimed such income to be lower than the profits and gains so deemed to be the profits and gains of his profession and his income exceeds the maximum amount which is not chargeable to income-tax in any previous year; or*

*(e) carrying on the **business or profession, other than a profession referred to in section 44AA(1)**, shall, if the provisions of sub-section (4) of section 44AD are applicable in his case and his income exceeds the maximum amount which is not chargeable to income-tax in any previous year,*

*get his accounts of such previous year audited by an accountant before the specified date and furnish by that date the report of such audit in the prescribed form duly signed and verified by such accountant and setting forth such particulars as may be prescribed.*

***(SUGGESTION FOR REDUCING/MINIMIZING LITIGATION)***

## 15. Section 44ADA- Computation of income on presumptive basis in case of notified professionals – Need for rationalisation of rate of presumptive income

### Provision of Law

The presumptive income of notified professions [professions referred to in section 44AA(1)] under section 44ADA is 50% of gross receipts or such higher sum claimed to have been earned by the assessee.

### Issue

Section 44ADA deems 50% of total gross receipts as presumptive income of professionals, which is on higher side especially since the provision is intended to cover professionals with gross receipts of upto Rs. 50 lakhs (Rs.75 lakhs, where the annual cash receipts do not exceed 5% of total gross receipts of the previous year). Due to this reason, many professionals do not opt for section 44ADA.

It may be noted that the Income Tax Simplification Committee, headed by Justice R V Easwar, has recommended the rate of 33.33% of the receipts as the income from profession.

### Suggestion

Section 44ADA may be suitably amended to deem 33.33% of Gross Receipts from profession as "Profits and gains of business and profession".

## 16. Sections 44AD & 44ADA – Special provisions for computation of profits and gains of eligible assessees engaged in eligible business and profession referred to in section 44AA(1) – Provisions of section 44ADA to be aligned with the provisions of section 44AD

**Provision of Law**

As per section 44AB, the following persons have to get their books of account audited by an accountant –

(a) every person, carrying on business shall, if his total sales, turnover or gross receipts, as the case may be, in business exceed or exceeds one crore rupees in any previous year (ten crore in cases where the aggregate receipts and aggregate payments during the previous year in cash does not exceed 5% of such receipts/payments, respectively).

(b) Every person carrying on profession shall, if his gross receipts in profession exceed fifty lakh rupees in any previous year

(c) Every person carrying on the business shall, if the profits and gains from the business are deemed to be the profits and gains of such person under section 44AE or section 44BB or section 44BBB, as the case may be, and he has claimed his income to be lower than the profits or gains so deemed to be the profits and gains of his business, as the case may be, in any previous year; or

(d) Every person carrying on the profession shall, if the profits and gains from the profession are deemed to be the profits and gains of such person under section 44ADA and he has claimed such income to be lower than the profits and gains so deemed to be the profits and gains of his profession and his income exceeds the maximum amount which is not chargeable to income-tax in any previous year; or

(e) Every person carrying on the business shall, if the provisions of sub-section (4) of section 44AD are applicable in his case and his income exceeds the maximum amount which is not chargeable to income-tax in any previous year,

get his accounts of such previous year audited by an accountant before the specified date and furnish by that date the report of such audit in the prescribed form duly signed and verified by such accountant and setting forth such particulars as may be prescribed

Section 44AD provides that, in case of an eligible assessee carrying on eligible business, a sum equal to 8%, or as the case may be, 6% of total turnover/gross receipts of the assessee in the previous year on account of such business or a sum higher than the aforesaid sum claimed to have been earned by the eligible assessee, shall be deemed to be the profits

and gains of such business chargeable to tax under the head "Profits and gains of business or profession".

Section 44ADA applies in case of an assessee, being an individual or a partnership firm other than a limited liability partnership who is a resident in India, and is engaged in a profession referred to section 44AA(1) and whose total gross receipts do not exceed fifty lakh rupees in a previous year. As per section 44ADA(1), in case of such notified professionals, a sum equal to fifty per cent of the total gross receipts of the assessee in the previous year on account of such profession or, as the case may be, a sum higher than the aforesaid sum claimed to have been earned by the assessee, shall be deemed to be the profits and gains of such profession chargeable to tax under the head Profits and gains of business or profession.

**Sub-sections (4) and (5) of section 44AD read as follows –**

(4) Where an eligible assessee declares profit for any previous year in accordance with the provisions of this section and he declares profit for any of the five assessment years relevant to the previous year succeeding such previous year not in accordance with the provisions of sub-section (1), he shall not be eligible to claim the benefit of the provisions of this section for five assessment years subsequent to the assessment year relevant to the previous year in which the profit has not been declared in accordance with the provisions of sub-section (1).

(5) Notwithstanding anything contained in the foregoing provisions of this section, an eligible assessee to whom the provisions of sub-section (4) are applicable and whose total income exceeds the maximum amount which is not chargeable to income-tax, shall be required to keep and maintain such books of account and other documents as required under sub-section (2) of section 44AA and get them audited and furnish a report of such audit as required under section 44AB.

**Sub-section (4) of section 44ADA reads as follows –**

(4) Notwithstanding anything contained in the foregoing provisions of this section, an assessee who claims that his profits and gains from the profession are lower than the profits and gains specified in sub-section (1) and whose total income exceeds the maximum amount which is not chargeable to income-tax, shall be required to keep and maintain such books of account and other documents as required under sub-section (1) of section 44AA and get them audited and furnish a report of such audit as required under section 44AB.

While the provisions offer simplified compliance for taxpayers, several practical concerns have emerged over time in its application.

### (i) Provisions of section 44ADA to be aligned with the provisions of section 44AD

**Issue**

Section 44ADA(4) requires notified professionals desiring to declare income lower than the presumptive income to maintain books of account and get them audited under section 44AB. This is not in alignment with the requirement of audit of accounts in clause (b) of section 44AB only for those professionals whose gross receipts in profession exceed Rs.50 lakhs.

In this context, it may be noted that section 44AD, which deals with presumptive taxation for eligible assessees engaged in eligible businesses, does not contain a provision akin to section 44ADA(4). Such assessees who do not opt for section 44AD at any point of time will have to get their books of account audited only if their turnover exceeds Rs.1 crore or Rs.10 crore, as the case may be.

**Suggestion**

It is suggested that the provisions of section 44ADA be aligned with that of section 44AD.

### (ii) Remuneration & interest to partners to be allowed as deduction

**Issue**

In case of firms, interest and remuneration paid to partners is not allowed as deduction from the presumptive income computed. Prior to amendment by the Finance Act, 2016, this deduction was allowed while computing presumptive income under section 44AD.

However, even now, section 44AE containing presumptive income provisions for assessees engaged in the business of plying and leasing goods carriages allows deduction for interest and remuneration to partners from the presumptive income computed thereunder, in the case of a firm.

**Suggestion**

It is suggested that payment to partners in nature of salary and interest may be allowed as deduction from presumptive income computed under section 44AD and 44ADA, subject to the conditions and limits specified in section 40(b).

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 17. Section 44AD – Special provisions for computation of profits and gains of eligible assessees engaged in eligible business – F&O and Speculative businesses to be excluded from the scope of section 44AD

### Provision of Law

Section 44AD(6) provides that the presumptive provisions contained in this section would not apply to a person carrying on profession referred to in section 44AA(1), a person earning income in the nature of commission or brokerage or a person carrying on agency business.

### Issue

In case of speculative business and F & O trading, profits can be determined directly from the reports generated from the stock exchanges where the trading takes place. Therefore, there is no need to maintain separate books of account to determine profits.

### Suggestion

It is suggested that since profits can be determined from the reports generated from the stock exchanges, these businesses can be excluded from the applicability of section 44AD, by including them in the list of exclusions in section 44AD(6).

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 18. Section 43B - Clarification regarding deduction of interest only on actual payment – Need to provide carveout for conversion in genuine cases like conversions under Insolvency and Bankruptcy Code, 2016

**Provision of Law**

Under section 43B, deduction for certain expenditure is allowable only on payment basis. Irrespective of the method of accounting followed by the assessee, deduction would be allowed only when the payment is made on or before the due date of filing of return.

**Issue**

*Explanations 3C, 3CA and 3D* of section 43B were amended by the Finance Act, 2022 w.e.f. 1.4.2023 to provide that a deduction of any sum, being interest payable on loan or borrowing from specified financial institution/NBFC/scheduled bank or a co-operative bank shall not be allowed even in cases where such interest is converted into a debenture or any other instrument by which liability to pay is deferred to a future date.

The aforesaid provision needs a relook especially in certain cases, it may cause inadvertent hardship to certain assessees. The amendment covers even the *bona fide* transactions within its ambit. This amendment is impacting debt ridden companies that enter into arrangement with financial institutions for recast of loan or outstanding interest into convertible, non-convertible instruments, equity, etc. as part of restructuring plans, despite being consented by the Banks or Financial Institutions. It may result in the situation where the deduction for interest on original loan converted into debenture (which then partakes the character of principal loan amount in the form of debenture) may never get allowed in perpetuity.

**Suggestion**

It is suggested that the amendment in section 43B pertaining to *Explanations 3C, 3CA and 3D* be reconsidered and further, there is a need to provide for a suitable carveout for conversion effected under the Corporate Insolvency Resolution Process ['CIRP'] under the Insolvency and Bankruptcy Code (IBC), 2016.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

# 1-D

# CAPITAL GAINS

## 19. Section 2(42A) - Period of holding of capital assets – Corresponding amendment required in proviso to section 50B(1) and clarification required in relation to period of holding of unlisted shares "offered for sale" to the public included in an IPO

Section 2(42A) was amended by the Finance (No.2) Act, 2024, to provide a holding period of "not more than 12 months" for all listed securities and "not more than 24 months" for all other assets. In effect, listed securities held for more than 12 months, and other assets held for more than 24 months would be long-term capital assets.

**Issues**

(i) Consequential amendment required in section 50B

Section 50B contains the special provisions for computation of capital gain in case of slump sale. The proviso to section 50B(1) provides that transfer under a slump sale of an undertaking held for "not more than 36 months" would be deemed to be capital gains from transfer of a short-term capital asset. Consequential amendment is required in the proviso to section 50B(1) to reduce the period of holding of the undertaking to "not more than 24 months" in line with section 2(42A) for deeming the transfer under the slump sale to be capital gains from transfer of a short-term capital asset.

**(ii) Period of holding of unlisted shares offered for sale to the public included in an IPO**

Section 55(2) provides for the meaning of "cost of acquisition" for the purposes of section 48 and 49. Clause (ac) thereof provides, in relation to a long-term capital asset being an equity share in a company or unit of an equity-oriented fund or a unit of a business trust referred to in section 112A, acquired before 1.2.2018, the cost of acquisition shall be higher of –

(i) the cost of acquisition of such asset; and

(ii) (ii) lower of –

(A) the fair market value (FMV) of such asset; and

(B) the full value of consideration received or accruing as a result of the transfer of the capital asset.

Item (AA) has been inserted and deemed to have been inserted w.e.f. 1.4.2018 by the Finance (No.2) Act, 2024 in sub-clause (iii) of clause (a) of the *Explanation* to section 55(2)(ac) to provide for the FMV of a capital asset, being an equity share in a company which is not listed on a recognised stock exchange as on 31.1.2018 but listed on such exchange subsequent to the date of transfer.

Since the shares are unlisted at the point of time of transfer, it is not clear whether the holding period for being treated as a long-term capital asset would be "more than 24 months" instead of "more than 12 months", being the holding period for assets referred to in section 112A.

**Suggestion**

It is suggested that –

i. consequential amendment is required in the proviso to section 50B(1) relating to slump sale to reduce the period of holding of the undertaking to "not more than 24 months" in line with section 2(42A) for the same to be treated as capital gains on transfer of a short-term capital asset.

ii. the minimum period of holding of unlisted equity shares which are "offered for sale" to the public included in an IPO, for being treated as a long-term capital asset, may be clarified.

***(SUGGESTION FOR REDUCING/MINIMIZING LITIGATION)***

## 20. Section 47 – Transactions not regarded as transfer – To include conversion of Convertible Notes into shares in section 47

### Provision of Law

Section 47(x) exempts conversion of bonds or debentures or debenture-stock or deposit certificate in any form, into shares or debenture of that company, from capital gains tax liability.

### Issue

Indian start-ups are allowed to issue Convertible Notes to resident individuals. RBI has permitted a person resident outside India to purchase Convertible Notes issued by an Indian start-up company for INR 25 lakhs or more in a single tranche (Notification No. FEMA.377/2016-RB, dated 10th January, 2017).

However, the conversion of Convertible Notes issued by an Indian start- up into shares or debentures is not specifically exempted from income-tax.

### Suggestion

It is suggested that to bring Convertible Notes at par with other instruments, a specific exemption may be provided for its conversion into equity.

***(SUGGESTION FOR REDUCING/MINIMIZING LITIGATION)***

## 21. Section 47(viab) - Transfer of capital asset consequent to amalgamation of foreign companies not regarded as transfer for capital gains – Consequent exemption to be provided in respect of transfer of shares by resident shareholders

### Provision of Law

Clause (viab) of section 47 provides exemption in respect of any transfer in a scheme of amalgamation, of a capital asset, being a share of a foreign company, which derives, directly or indirectly, its value substantially from the share or shares of an Indian company, held by the amalgamating foreign company to the amalgamated foreign company.

### Issue

There is, however, no clause which provides consequent exemption in respect of transfer of shares by the resident shareholders of amalgamating foreign company in consideration of allotment of shares of amalgamated foreign company. This appears to be an inadvertent omission, since in case of exemption u/s 47(vi) in respect of transfer of capital asset in a scheme of by an amalgamating company to the amalgamated company, where the amalgamated company is an Indian company, consequent exemption has been provided u/s 47(vii) in the hands of the shareholders of the amalgamating company for transfer of shares of amalgamating company in consideration of allotment of shares of amalgamated company.

Further, transfer in a scheme of business reorganization of a capital asset, being a share of a foreign company, which derives, directly or indirectly, its value substantially from the share or shares of an Indian company should also be exempt under section 47. Business reorganization may be defined to mean the reorganization of business, otherwise than by way of amalgamation or demerger of foreign companies.

### Suggestion

New clauses may be inserted in section 47 to provide for:

(i) Consequent exemption in respect of transfer of shares by the resident shareholders of the amalgamating foreign company if transfer is made in consideration of the allotment to him of any shares or shares in the amalgamated foreign company.

(ii) exemption in respect of transfer in a scheme of business re-organisation of a capital asset, being a share of a foreign company, which derives, directly or indirectly, its value substantially from the share or shares of an Indian company.

***(SUGGESTION FOR RATIONALIZING PROVISIONS OF DIRECT TAX LAWS)***

## 22. Section 47(xiiib) – Conversion of a private limited company or an unlisted public company to an LLP not a transfer for capital gains – Relaxation of certain conditions

### (a) Need for Relaxation of turnover criterion

**Provision of Law**

Section 47(xiiib) provides that no capital gains tax is payable on conversion of a private limited or unlisted public company into LLP subject to certain conditions. Clause (e) of the proviso thereto states that this provision will apply only if the total sales, turnover or gross receipts in the business of any of the three preceding years does not exceed Rs.60 lakhs.

**Issue**

Since this is a provision intended to facilitate conversion of private limited companies and unlisted companies into LLPs, ideally, there should be no restriction on the turnover to avail the benefit of section 47(xiiib). It may also be noted that the parent Act i.e. Limited Liability Partnership Act 2008, allows this conversion without any such restrictions.

**Suggestion**

It is suggested that, with a view to popularize the concept of LLP and also in view of the fact that such provision should apply to all cases of revenue neutral conversions from one form of entity to another form of entity, there should be no threshold on turnover, to avail the benefit under section 47(xiiib)

Alternatively, the limit of sixty lakh rupees may be substantially enhanced to ten crore rupees.

### (b) Increase in threshold of total assets and clarification relating to meaning of "value of total assets as appearing in the books of account"

**Provision of Law**

Section 47(xiiib) provides that no capital gains tax is payable on conversion of a private limited or unlisted public company into LLP subject to certain conditions. Clause (ea) of the proviso thereto states that this provision will apply only if the total value of the assets as appearing in the books of account of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed Rs.5 crore.

**Issue**

LLP is a preferred form of organization for smooth conduct of business. Accordingly, section 47(xiiib) provides for an exemption enabling smooth conversion, subject to compliance with the conditions. There was a case for making the exemption more liberal by relaxing the turnover limit which is one of the present conditions. However, conversion will become all the more difficult as a result of an additional condition which will deny exemption in a case where the company was possessed of total assets worth Rs. 5 crore in any of the 3 years.

The expression "value of total assets appearing in the books of accounts" is not defined and may create certain interpretational issues such as whether status of assets is to be seen on balance sheet date or even one day's presence during the year will be considered, even if asset no longer exists with the assessee as on balance sheet date. Also, whether 'Miscellaneous Expense' as an item reflected on balance sheet will constitute an asset, treatment of advance tax paid shown on asset side (with corresponding provisions for tax on liability side), etc. are the other issues which need to be addressed.

**Suggestion**

In view of the aforesaid, it is suggested that -

(i) the condition of asset base being less than Rs. 5 crore be rationalized and increased to Rs 10 crore.

(ii) the meaning and scope of the term 'value of total assets as appearing in the books of account' be clarified to provide certainty and reduce litigation.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 23. Sections 47(x) & (xa) and 49(2A) - Capital Gain on Conversion of Foreign Currency Exchangeable Bonds (FCEB) and other bonds into shares of any company – Need for amendment in section 2(42A) to include period of holding of bonds

### Provisions of Law

Section 47(xa) read with section 49(2A) effectively provide that conversion of FCEB in to shares of any company will not give rise to capital gain and for the purpose of computing capital gain arising on sale of such shares at subsequent stage, cost of acquisition shall be taken as the relevant part of cost of FCEB.

### Issue

There is, however, no corresponding provision for taking holding period of the shares from the day of acquisition of the Bonds [FCEB]. Likewise, difficulty arises in case of conversion of debentures and other bonds in to shares for which also, there is a similar provision in section 47(x).

### Suggestion

It is suggested that appropriate amendment may be made in section 2(42A) to provide that the period of holding of such shares should be taken from the date of acquisition of FCEB/debentures/other bonds and not from the date of allotment of shares.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 24. Section 45(5A) - Tax implications to Individuals/HUFs under Joint development agreements (JDAs) – Extension of application of this provision to other assessees, defining the term "consideration" and reckoning of time period for the purpose of sections 54/54EC/54F etc. from the date of issue of completion certificate

### Provision of Law

Section 45(5A) is applicable where capital gains arises to an assessee, being an individual or HUF, from the transfer of a capital asset, being land or building or both, under a joint development agreement. The capital gains is deferred to the previous year in which the certificate of completion for the whole or part of the project is issued by the competent authority.

Section 194-IC provides for deduction of tax at source@10% by any person responsible for paying to a resident any sum by way of consideration, not being consideration in kind at the time of credit of such sum to the account of the payee or at the time of payment, whichever is earlier.

### Issues

(i) Section 45(5A) is applicable only to individuals and HUFs. It may be extended to all assessees.

(ii) The term "consideration" has not been defined in either section 45(5A) or section 194-IC.

(iii) For capital gains *inter alia* from JDAs, the exemption provisions are contained in sections 54, 54F, 54EC. However, the time limits in the said sections have not been extended w.r.t. section 45(5A). Due to lack of funds, sometimes, in case of joint development agreements, there is a need to provide clarity that the time limit would be reckoned from the date of completion of the property for the purpose of claiming exemptions from capital gains under the aforesaid sections.

### Suggestion

It is suggested that –

(i) the provisions of section 45(5A) be extended to capital gains arising to other assessees also.

(ii) the term "consideration" may be defined for the purposes of section 45(5A) and section 194-IC.

(iii) the time limit for the purpose of exemption provisions of section 54, 54EC and the like be reckoned from the date of receipt of the completion certificate of the property which may be taken as date of transfer as well. In the alternative, the date of transfer may be the date of issuance of completion certificate.

## 25. Section 49(7) - Cost of Acquisition on subsequent sale of share of property in Joint Development Agreement – Stamp duty value of the share of property forming part of full value of consideration under section 45(5A)

### Provision of Law

As per section 49(7), on subsequent sale of share of land or building or both given to the assessee as full value of consideration, the cost of acquisition shall be the amount which is deemed as full value of consideration under section 45(5A) of the Act.

### Issue

The full value of consideration under section 45(5A), however, includes both the Stamp Duty Value (SDV) of the share of land or building or both as well as consideration received in cash/cheque/draft etc.

### Suggestion

Section 49(7) may be amended to mention that on subsequent sale of share of land or building or both, the cost of acquisition shall be deemed to be the stamp duty value of such share of land or building or both forming part of the full value of consideration u/s 45(5A).

***(SUGGESTION FOR RATIONALIZING THE PROVISIONS OF DIRECT TAX LAWS AND IMPROVING TAX COLLECTION)***

## 26. Section 48 - Mode of computation of long-term capital gains and in section 112 relating to the rate of tax – Option be provided to taxpayer to pay tax@20% on LTCG computed with indexation benefit or pay tax@12.5% on LTCG computed without indexation benefit, to ensure equity

Section 48 requires computation of the income chargeable under the head "Capital gains" by deducting, *inter alia*, the cost of acquisition of the asset and the cost of any improvement of the capital asset from the full value of the consideration received or accruing as a result of the transfer of such capital asset.

Where long-term capital gain arises from transfer of a long-term capital asset before 23.7.2024, the second proviso to section 48 provided for reduction of "**indexed cost of acquisition**" and "**indexed cost of improvement**" from the full value of consideration instead of "cost of acquisition" and "cost of improvement". The benefit of indexation was available in respect of cost of long-term capital assets transferred before 23.7.2024, other than certain assets, like assets referred to in section 112A. The long-term capital gains so computed by considering the indexed cost of acquisition/improvement is chargeable to tax@20% under section 112.

Section 48 read with section 112 was amended by the Finance (No.2) Act, 2024 to remove the indexation benefit while simultaneously reducing the rate of tax to 12.5% w.e.f. 23rd July, 2024. On account of this amendment, any transaction of transfer of capital assets on or after July 23rd, 2024 would be chargeable to tax@12.5% on the difference between the sale price and cost of purchase/FMV as on 1.4.2001, as the case may be, without any indexation benefit. However, in case of transfer effected on or after July 23rd, 2024, of a long-term capital asset, being land or building or both, which was acquired by a resident individual or a HUF before July 23rd, 2024, while computing tax liability u/s 112, the excess tax computed on long-term capital gains without indexation under the new regime over the tax computed in accordance with the provisions under the earlier regime would be ignored.

**Issue**

(i) The option of computing tax on long-term capital gains under the old and new regime and choose the more beneficial one is available to resident individuals and HUFs who acquired land or building or both, for transfer of such land or building or both effected on or after 23.7.2024 by virtue of the second proviso to section 112(1)(a). It is not available for transfers effected before that date i.e., transfers

effected during the period 1.4.2024 to 23.7.2024. This option, should, ideally be available for transfers effected from 1.4.2024.

(ii) The investment to be made in residential house for availing benefit of section 54 or in bonds of NHAI/RECL for availing benefit of section 54EC would be lower where long-term capital gains is computed giving indexation benefit as per the provisions existing before 23.7.2024. Accordingly, in respect of transfer of land or building or both acquired by resident individuals and HUFs before 23.7.2024, where the transfer is effected on or after 23.7.2024, benefit of re-investment of a lower amount in another residential house/bonds of NHAI/RECL and paying tax@20% of capital gains computed with indexation benefit as per section 112 would be available. However, in respect of transfer of land or building or both acquired by resident individuals and HUFs on or after 23.7.2024, this benefit is not available. Furthermore, the capital gains computed without indexation benefit would always be much higher than the capital gains computed with indexation. Therefore, there is a need to increase the threshold limit of Rs.50 lakhs in section 54EC.

Let us take an example of capital gains arising on sale of land acquired by an individual on 1.4.1999 at a cost of Rs.10 lakhs (FMV as on 1.4.2001 – Rs.13 lakhs) and transferred on 12.10.2024, the details of which are as follows.

| **Column 1** | | **Column 2** | |
|---|---|---|---|
| **Computation of LTCG forming part of TI for A.Y.2025-26** | | **Computation of LTCG as per the provisions of law prior to amendment by the Finance (No.2) Act, 2024** | |
| **Particulars** | **Rs.** | **Particulars** | **Rs.** |
| Full value of consideration | 98,50,000 | Full value of consideration | 98,50,000 |
| *Less:* Expenses on transfer | 1,31,000 | *Less:* Expenses on transfer | 1,31,000 |
| Net Consideration | 97,19,000 | Net Consideration | 97,19,000 |
| *Less:* Cost of acquisition | 13,00,000 | *Less:* Indexed Cost of acquisition [Rs.13,00,000 x 363/100] | 47,19,000 |
| | 84,19,000 | | 50,00,000 |
| *Less:* Exemption u/s 54EC | | *Less:* Exemption u/s 54EC | |

| | | | |
|---|---|---|---|
| | 50,00,000 | | 50,00,000 |
| Long-term capital gains (included in total income) | 34,19,000 | Long-term capital gains computed as per the provisions of income-tax law prior to amendment by the Finance (No.2) Act, 2024 | - |
| Tax@12.5% on LTCG of Rs.34.19 lakhs | 4,27,375 | Tax@ 20% on LTCG of Nil | - |

It can be seen that although the LTCG included in Gross Total Income works out to Rs.34.19 lakh, no tax is payable since the amount of investment in bonds of NHAI/RECL required for exemption of LTCG computed under the provisions of law as it stood prior to amendment by the Finance (No.2) Act, 2024 is Rs.50 lakhs, which if invested, there would be no tax liability as per section 112.

However, in case of a long-term capital asset, being residential house/land or building or both, acquired on or after 23.7.2024, since the option for paying tax under the erstwhile provisions is not available, and the long-term capital gains computed as per the current provisions without indexation would be higher, the threshold for investment u/s 54 and 54EC may be suitably increased. In the above example, if the long-term capital gains computed in column 1 was in respect of land acquired on or after 23.7.2024, say, on 24.7.2024 and transferred on say, 30.7.2026, then, the amount of investment required in section 54EC for the capital gains to be fully exempt in the A.Y.2027-28 is Rs.84.19 lakhs, whereas the maximum permissible investment is only Rs.50 lakhs.

(iii) Though resident individuals and HUFs can avail the benefit of paying lower taxes/no taxes on account of applying the erstwhile indexation provisions, however, if the resultant figure is a loss, the same cannot be set-off or carried forward, since the erstwhile provisions can be applied only for computing tax liability and not for computation of capital gains to be included in total income.

**Suggestions**

It is suggested that -

(i) The option u/s 112 may be given in respect of transfer of long-term capital asset, being land or building or both, by a resident individual/HUF at any time during the P.Y.2024-25 (not only for transfers effected on or after 23.7.2024, but also for transfers effected before that date).

(ii) If the resultant figure on applying the erstwhile provisions on indexation is a loss, suitable provisions may be introduced to permit set-off/carry forward and set-off of such loss as per the provisions of the Act.

(iii) The threshold limits for exemption u/s 54 and 54EC in respect of long-term capital gains reinvested in residential house and bonds of NHAI/RECL be suitably increased in respect of transfer of long-term capital asset acquired on or after 23.7.2024, since capital gain has to be computed without indexation benefit, which would be much higher.

The threshold limit of Rs.50 lakh in case of section 54EC may be substantially enhanced to Rs.2 crore, considering that the limit was fixed in 2007. Also, these funds are used for infrastructure development and contribute to the welfare of the society.

(iv) The CBDT may come out with FAQs showing computation of long-term capital gains and tax liability thereon in different scenarios with the help of examples/illustrations.

***(SUGGESTION FOR RATIONALIZING THE PROVISIONS OF DIRECT TAX LAWS)***

**27. (i) Section 50C/43CA/56(2)(x) – Stamp duty value of land or building or both deemed as full value of consideration in the hands of the seller – Difference between stamp duty value and actual consideration is also income of buyer – Issue of double taxation to be addressed**

**(ii) Section 50C -10% tolerance band prescribed in section 50C(1) with respect to stamp duty value - Clarification on applicability of 10% tolerance band to value determined by Valuation Officer under Section 50C(2)**

**Provisions of law**

(i) Stamp duty value of land or building or both is deemed as the full value of consideration u/s 50C/43CA, as the case may be, in the hands of the seller. Section 56(2)(x) brings to tax the difference between the stamp duty value of land or building or both and the actual consideration as income of the buyer. There is a tolerance band of 10% in these sections.

(ii) As per the third proviso to section 50C(1), where the value adopted or assessed or assessable by the stamp valuation authority does not exceed 110% of the consideration received or accruing as a result of the transfer, the consideration so received or accruing as a result of the transfer, shall, for the purposes of section 48, be deemed to be the full value of consideration received.

**Issue**

(i) There is double taxation to the extent of tax on difference between the stamp duty value and actual consideration. This is subject to tax both in the hands of the buyer and seller.

(ii) A tolerance band of 10%, therefore, applies when the stamp duty value is determined by the Stamp Valuation Authority as per section 50C(1). However, it is not clear whether the 10% tolerance band is also applicable to the value determined by the Valuation Officer, on a reference being made by the Assessing Officer under section 50C(2).

When the valuation is referred to the Valuation Officer and the officer determines a value lower than the stamp duty value, this lower value is taken as the full value of consideration. However, it is not clear whether the 10% tolerance band would also apply to such valuation.

**Suggestions**

It is suggested that

(i) the concern of double taxation both in the hands of the seller under section 50C/43CA and the buyer u/s 56(2)(x) of tax payable on the difference between stamp duty value and actual consideration be addressed.

(ii) the proviso to section 50C(1) be removed and a proviso to section 50C as a whole be inserted after section 50C(3) which reads as follows -

*"Where the value adopted or assessed or assessable by the stamp valuation authority or the value determined by the Valuation Officer, as the case may be, does not exceed 110% of the consideration received or accruing as a result of the transfer, the consideration so received or accruing as a result of the transfer, shall, for the purposes of section 48, be deemed to be the full value of consideration received."*

***(SUGGESTION FOR RATIONALISATION OF THE PROVISIONS OF TAX LAWS AND REDUCING/MINIMISING LITIGATION)***

## 28. Section 54EC – Exemption of long-term capital gains on transfer of land or building or both if invested in specified bonds – Certain concerns to be addressed

### (a) Time Limit for investment in specified bonds – Suggestion to extend upto the due date of filing return of income

**Provision of Law**

Under section 54EC, long-term capital gains from transfer of land or building or both is exempt, if such gains are re-invested in specified bonds (for example, NHAI or RECL bonds) within 6 months from the date of transfer.

**Issue**

The time limit for investment in specified bonds is presently 6 months from the date of transfer.

(i) In a number of transactions, there is some difference in dates of actual handing over of possession, submission of documents for registration of transfer, actual date of registration and even a subsequent modification of registered document due to demand of additional stamp duty. All these dates, though may fall in the same year but still may differ from each other, creating an unnecessary dispute regarding actual date of transfer and thereby time limit of 6 months. If the date of investment in specified bonds is made upto the due date of filing return u/s 139(1), such disputes can be avoided.

(ii) Bringing the time limit upto the due date of filling of ITR shall also bring parity with section 54/54B/54F etc. where assessee is permitted to deposit the money in Capital Gains Account Scheme upto the due date of filing of ITR. In fact, assessee would be in a better position to take a call as to which exemption option is better suited for him.

(iii) In many cases, the assessee is not aware about exemption provision and comes to know about it only when he approaches his/her tax consultant at the time of filling of return of income u/s 139(1). By this time, 6 months period is already over and thus, the assessee inadvertently loses the benefit of exemption.

(iv) The time limit expires exactly at 6 months from the date of transfer. Due to this, even an otherwise aware assessee may miss it unintentionally.

**Suggestion**

It is suggested to amend section 54EC so that time limit for investment in specified bonds may be allowed upto the due date of filing of return of income under section 139(1).

**(b) Capital gains exemption on investment in Specified Bonds during the financial year – Suggestion to remove of first proviso and increase in threshold limit to Rs.2 crore**

**Provisions of Law**

The first proviso to section 54EC(1) provides that investment made in long term specified asset (bonds) during the financial year should not exceed Rs.50 lakhs.

In furtherance of the first proviso to section 54EC(1), the second proviso clarifies that the investment made by an assessee in the long-term specified asset, from capital gains arising from ***transfer of one or more original assets***, during the financial year in which ***the original asset or assets*** are transferred and in the subsequent financial year does not exceed Rs.50 lakh.

**Issue**

The change was made to plug the revenue leakage and to clarify the real intent of the law. Since the second proviso is in furtherance of the first proviso, it may cause hardship in genuine cases where investment has to be made in long term specified asset in respect of two previous years in a single financial year. For example, an assessee transferring a land or building in February, 2025 (P.Y. 2024-25) may invest in NHAI/RECL bonds either in the P.Y. 2024-25 or in the P.Y.2025-26 (upto August, 2025) for claiming exemption under section 54EC. However, if he transfers another long-term capital asset, being land or building, in the P.Y. 2025-26 also, he will not be able to invest in 54EC bonds, since exemption will not be available to him due to applicability of first proviso to section 54EC.

**Suggestion**

Considering that the second proviso takes care of the true intent of the law, and the first proviso to section 54EC(1) imposes further restriction, thereby causing hardship to the genuine taxpayers, it is suggested that section 54EC be amended to substitute the first proviso with the second proviso.

Further, considering the inflation factor and the Government's objective of promoting investment in infrastructure and considering that the capital gain computed without indexation benefit would be higher, it is suggested that the said limit of Rs.50 lakhs may be raised to Rs. 2 crore.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 29. Section 54/54F- Deduction for re-investment of capital gains/net consideration in long-term capital asset, being residential house – Restriction of Rs.10 crore for investment in new residential house be removed in section 54, minimum period of holding of new asset to be reduced to 24 months and uniform consequence on transfer of new capital asset before the said period

### Provisions of Law

Section 54 provides for deduction of long-term capital gain on transfer of residential house, to the extent that the same is re-invested in purchase or construction of one or two residential house(s) in India within the prescribed time from the date of transfer. Amount re-invested in purchase of two residential houses in India will be permissible as deduction u/s 54 only when the amount of capital gain does not exceed Rs. 2 crore.

Section 54F provides deduction of long-term capital gains on transfer of a capital asset, not being a residential house, if the net consideration is re-invested in purchase or construction of one residential house in India within the time prescribed from the date of transfer.

### Issue

Section 54 provides for capital gain exemption on transfer of residential house and reinvestment in another residential house(s) in India whereas section 54F provides for capital gain exemption on transfer of long-term capital asset, other than residential house, where the net consideration is re-invested in a new residential house in India.

There is a restriction of Rs.10 crore on the investment in new residential house both under section 54 and under section 54F for the purpose of exemption thereunder.

Also, if the new asset is sold or transferred within 3 years, the manner in which the earlier exempted capital gains is subject to tax varies in these sections. In sections 54,54B and 54D, the earlier exempted capital gains is reduced from the cost, whereas sections 54EC and 54F deems the capital gains not charged to tax earlier as income chargeable to tax of the year in which the transfer of the new asset takes place.

Moreover, whereas the period of holding of an asset to be treated as long-term has reduced from "more than 36 months" to "more than 24 months", there has been no corresponding amendment in the minimum period of holding of the new asset in sections 54 to 54F.

**Suggestions**

It is suggested that -

(i) Since section 54 provides for exemption in respect of long-term capital gains on transfer of residential house, which is re-invested in another residential house, the restriction that the amount invested in excess of Rs.10 crore will not be eligible for deduction be removed.

(ii) The cap of Rs. 2 crore capital gain in section 54 for reinvestment in two residential houses in India may be removed or alternatively, may be increased to atleast Rs. 10 crore.

(iii) The minimum period of holding of new asset be reduced from 3 years to 2 years in line with the minimum period of holding of an asset to be treated as long-term capital asset under section 2(42A).

(iv) In case of the new asset is not held for a minimum period of 2 years, the capital gains exempt earlier should be deemed as income chargeable to tax in the year of transfer of the new asset. This should be the consequence of transfer of new asset before the minimum period of 2 years in all sections (sections 54/54B/54D/54EC/54F).

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 30. Tracking the un-spent portion of capital gain deposit – Levy of TDS at the time of withdrawal

### Issue

At present, there is no mechanism provided in the Act/Rules for tracking the un-spent portion of capital gain deposit. Only when the assessees want to withdraw the money (otherwise than for house construction), some banks insist on tax clearance certificate. The assessees are also finding it difficult to obtain the tax clearance certificate.

### Suggestion

It is suggested that the relevant Rules/Act can be amended to provide that the un-spent amount can be released by the bank after deducting 20% thereof which can be remitted to the Government by way of TDS.

***(SUGGESTION FOR IMPROVING TAX COLLECTION)***

## 31. Sections 2(22)(f), 10(34A), 46A and 115QA - Tax on distributed income of a domestic company for buy-back of shares – Need for re-consideration

Sub-clause (f) has been inserted in section 2(22) w.e.f. 1st October, 2024, to include any payment made by a company on purchase of its own shares from a shareholder in accordance with the provisions of section 68 of the Companies Act 2013 as dividend. The amounts received by the shareholder on buy-back of the shares in accordance with the Companies Act, 2013 would be considered as dividend and would be subject to tax in the hands of the shareholder as dividend at the applicable normal tax rates. Since, the shares would be extinguished on buyback, it will also amount to transfer of those shares, for the purpose of which the consideration would be treated as Nil; and the resultant loss would be a capital loss.

**Issue**

Artificially breaking of income on buy back into dividend and capital loss is not in line with the principles set by other Central Acts like the Companies Act, 2013.

While the amounts received on buyback are being taxed at the rate of 30% (assuming that the recipient is an individual having total income above 15 lakhs), the long-term capital loss can be only be set-off against the long-term capital gains, if any, which is otherwise taxable@12.5% under the proposed capital gain tax provisions.

**Suggestion**

It is suggested that the capital loss may be permitted to be set off against the said dividend income.

***(SUGGESTION FOR REDUCING/MINIMISING LITIGATION)***

# 1-E

# INCOME FROM OTHER SOURCES

## 32. Section 56(2)(x) - Definition of the term relative in Explanation to Section 56(2)(vii) – Need for expansion in scope of the definition

**Provision of Law**

Under the existing provisions of section 56(2)(x), any sum or property received by an individual or HUF for inadequate consideration or without consideration is deemed as income and is taxed under the head 'Income from other sources'. However, in case of any individual, receipts from specified relatives are excluded from the purview and hence, are not taxable.

As per clause (e) of Explanation to section 56(2)(vii), "relative" means –

(i) in case of an individual -

(A) spouse of the individual;

(B) brother or sister of the individual;

(C) brother or sister of the spouse of the individual;

(D) brother or sister of either of the parents of the individual;

(E) any lineal ascendant or descendant of the individual;

(F) any lineal ascendant or descendant of the spouse of the individual;

(G) spouse of the person referred to in items (B) to (F).

(ii) in case of a Hindu undivided family, any member thereof.

**Issue**

It may be noted that, in relation to an "individual", the term relative, as it stands at present includes brother or sister of either parents of the individual but does not include children of brother or sister of the individual or spouse of individual. Also, maternal grandparents are not included in the meaning of lineal ascendant or descendant of the individual. This may not be the legislative intent. Further, in the case of HUF, relative means a member thereof. However, relatives of members are not included in the said definition.

As per clause (b) of Explanation to section 56(2)(x), the expression property shall have the same meaning as assigned to it in clause (d) of Explanation to clause (vii) and shall include virtual digital asset. Clause (vii) of section 56(2) is not relevant since A.Y.2017-18. Therefore, the expression "property" may be defined in clause (x) itself, by including "virtual digital asset" as item (x) after bullion. This will ensure that virtual digital asset, which is a capital asset is included in the definition of property.

**Suggestion**

It is suggested that –

(i) Lineal descendants of brothers and sisters of self and spouse may also be included in the definition of "relative" in line with Clause (vii) of Explanation 1 to section 13. Also, maternal grandparents may be included in the definition of "relative".

(ii) The expression "property" may be defined in clause (x) itself, by including "virtual digital asset" as item (x) after bullion. This will ensure that virtual digital asset, which is a capital asset is included in the definition of property.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 33. Section 56(2)(x) – Receipt of property without consideration/inadequate consideration – Recipient to be given an opportunity to substantiate the variation - Permissible deviation of 10% for receipt of immovable property to be extended to other properties also

**Provision of Law**

Section 56(2)(x) brings to tax sum of money or value of property received without consideration.

It also brings to tax the difference between –

(i) the stamp duty value and the actual consideration, where immovable property is received for inadequate consideration, and the difference between the stamp value and the consideration exceeds Rs.50,000 or 10% of actual consideration, whichever is higher.

(ii) the aggregate fair market value and the actual consideration, where property, other than immovable property, is received for inadequate consideration, and the difference between the aggregate fair market value and the consideration exceeds Rs.50,000.

**Issue**

Section 56(2)(x) is an anti-abuse provision intending to curb tax avoidance. Such provisions should not get attracted where there is no possibility of any tax avoidance. However, the language of the section as presently worded does not allow any scope for explanation of a transaction being undertaken in a particular manner which may be at variance with the deemed value resulting from mechanical application of the rules.

This may have certain unintended results:

(i) Section 56(2)(x) may get attracted to genuine transaction not leading to any tax avoidance.

(ii) The mechanical application of deemed value may create additional tax liability based on historical costs with no correlation with the current economic value.

No one valuation method or a price can be said to fairly deal with multifarious commercial realities of transactions even when no tax avoidance is involved. The Income-tax Act, 1961 itself has recognised it in several other provisions which are anti abuse provisions. For example, Section 50C which was introduced to check undervaluation in context of transactions in immovable properties, provides an option to the assessee to present a case as to why stamp duty valuation is unjustified. Further, an inbuilt tolerance of upto 10% has been permitted for acceptance of transaction value. Incidentally, section 56(2)(x) incorporates this principle only for immovable property transaction but not for other transactions.

There are many genuine reasons for transaction to happen at a price in variance to a mechanical rule:

(i) the transfer of property may be under stressed conditions (like covid created circumstances),

(ii) the volume of transaction and contractual terms may be at variance with what has been assumed.

(iii) the special characteristics and nature of transaction like a case of bulk deal undertaken off exchange.

(iv) historical costs may not reflect the present economic value of the property.

In such situation, to burden the taxpayer with tax liability based on an artificial construct with no recourse to even present the matter for consideration by the tax authorities and automatic presumption of undervaluation may not be justified.

Considering the wide scope of transactions covered under section 56(2)(x), it is of utmost importance that there is an enabling provision in the section allowing the assessee an opportunity to substantiate that the transaction price variation is justified. It is ultimately for the tax department to analyse and examine whether the explanation offered is satisfactory or not.

**Suggestion**

It is suggested that section 56(2)(x) may be amended to enable the person in receipt of property to offer explanation regarding the inadequacy of consideration, if any, vis-à-vis the fair market value as determined in prescribed manner and if such an explanation is found satisfactory by the Assessing Officer, then, the provisions of the said section shall not apply to such transaction.

Also, the permissible deviation of 10% from the actual consideration of immovable property may be extended to receipt of property, other than immovable property, for inadequate consideration.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 34. Section 56(2)(x) read with Rule 11UA(1)(a) – Manner of determination of value of jewellery – Clarification relating to manner of determination of value of bullion

### Provision of law

As per *Explanation* to section 56(2)(x) read with clause (b) of *Explanation* to 56(2)(vii), fair market value of a property, other than immovable property, means the value determined in accordance with the method as may be prescribed.

As per *Explanation* to section 56(2)(x) read with clause (d) of *Explanation* to 56(2)(vii), "Property" means the following capital asset of the assessee, namely –

(i) Immovable property, being land or building or both;
(ii) Shares and securities
(iii) Jewellery
(iv) Archaeological collections
(v) Drawings
(vi) Paintings
(vii) Sculptures
(viii) Any work of art
(ix) Bullion

Rule 11UA lays down the method for determination of FMV of a property, other than immovable property. Clause (a) of Rule 11UA(1) lays down the manner of determination of value of jewellery, clause (b) lays down the the manner of determination of value of archaeological collections, drawings, paintings, sculptures and any work of art and clause (c), the manner of determination of value of shares and securities. However, there is no separate clause laying down the manner of determination of bullion.

### Issue

Though jewellery and bullion are separately listed out in the definition of property for the purpose of section 56(2)(x), there is no separate clause in Rule 11UA(1) for valuation of bullion. It is not clear whether clause (a) laying down the manner of determination of value of jewellery will apply for bullion also.

### Suggestion

It is suggested that -

(i) Clause (a) of Rule 11UA providing for the manner of determination of valuation of jewellery be made applicable for valuation of bullion also; or

(ii) A separate clause be inserted in Rule 11UA providing for the manner of determination of valuation of bullion.

***(SUGGESTION FOR REDUCING/MINIMISING LITIGATION)***

## 35. Section 56(2)(x) – Exclusion from applicability provided in respect of sum of money or property received - Need for inclusion of certain clauses of section 47 in sub-clause (IX) of the proviso to section 56(2)(x)

### Provision of Law

Section 56(2)(x) contains provisions related to charging of income to tax where a person receives any money, immovable property or property other than immovable property without consideration or with inadequate consideration.

The proviso to section 56(2)(x) provides the cases to which this clause would not apply. Sub-clause (IX) of the proviso to section 56(2)(x) lists certain clauses of section 47 to which this section would not be applicable.

### Issue

Certain clauses of section 47, however, seem to be missed out even though they specially related to conversions. Consequently, even though such transactions are not regarded as transfer and capital gain would not be attracted, however, if it includes immovable property or property other than immovable property (eg shares), they could be covered u/s 56(2)(x). These clauses are as follows:

- Clause (xiii) – Transfer of a capital asset on succession of firm by a company
- Clause (xiiib) – Transfer of a capital asset by a private company or unlisted public company to a LLP on conversion of company into LLP
- Clause (xiv) – Succession of sole proprietorship by a company and consequent transfer of capital asset to the company.

Also, section 56(2)(x) is an anti-abuse provision intending to curb tax avoidance. It should not be levied where clearly there is no tax avoidance. However, section 56(2)(x) may get attracted even in case of genuine transactions not leading to any tax avoidance like slump sale and conversion of preference shares/debentures.

### Suggestion

It is suggested that -

(i) sub-clause (IX) of the proviso to section 56(2)(x) may be amended to include reference to clauses (xiii), (xiiib) and (xiv) of section 47

(ii) slump sale and conversion of preference shares/debentures be specifically excluded from ambit of section 56(2)(x)

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 36. Section 2(22)(e) – Deeming loan or advance to a shareholder who is the beneficial owner of shares holding not less than 10% of voting power or to a concern in which such shareholder has substantial interest as dividend – Need for certain exclusions and increase in the threshold % of voting power

### Provision of Law

As per section 2(22)(e), dividend includes any payment by a company, not being a company in which the public are substantially interested, of any sum (whether as representing a part of the assets of the company or otherwise), by way of advance or loan to a shareholder, being a person who is the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) holding not less than ten per cent of the voting power, or to any concern in which such shareholder is a member or a partner and in which he has a substantial interest (hereafter in this clause referred to as the said concern) or any payment by any such company on behalf, or for the individual benefit, of any such shareholder, to the extent to which the company in either case possesses accumulated profits.

### Issues

(i) The applicability of this deeming provision in the following cases require reconsideration –

- where loans and advances are given on proper interest and re-payment terms; or
- when loans and advances are given in connection with the business needs or in the ordinary course of business.

Avoidable litigation has arisen even in cases where the advances are given for the purpose of purchase of goods in the ordinary course of business.

(ii) The limit of 10% shareholding, which can establish nexus with the concern is considered in practice to be considerably low. It is quite possible that an investor like PE investor or a passive investor may create such a situation without the concerns being aware of the same. Further, the requirement is beneficial holding in the concern. It may not be possible for a company giving loan to ascertain the beneficial holding of its shareholders in another concern. The company will be dependent wholly on the certification of the shareholder.

(iii) Also, it needs to be spelt out in an explicit manner whether the amount will be chargeable in the hands of the concern or in the hands of the concerned shareholder, where the loan is given to a concern in which the shareholder is a member or partner and in which he has substantial interest.

**Suggestion**

It is suggested that:

(i) The continuance of the provision itself in the current form may be re-considered. The provision was introduced at a time the tax rates were materially substantial, governance was difficult and closely held companies were almost universally governed by a singular family.

(ii) Assuming it is not re-considered, by way of rationalisation, the applicability may be restricted to a case where the shareholder who is the beneficial owner of shares holding not less than 25% of voting power or to a concern in which such shareholder has substantial interest. Also, it needs to be clarified as to whether the amount of dividend should be taxed in the hands of the concerned shareholder or in the hands of the concern.

(iii) Loans and advances which are given on terms which are at arm's length and / or reasonable may be excluded from the scope of section 2(22)(e).

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

# 2

# INCOME OF OTHER PERSONS INCLUDED IN ASSESSEE'S TOTAL INCOME

## 37. Section 60 - Transfer of income where there is no transfer of assets - Need for exception in case of transfer of income to a charitable trust registered u/s 12AB without transfer of asset, where the assignment of income is for a period of atleast 5 years.

### Provision of Law

Section 60 provides that all income arising to any person by virtue of a transfer whether revocable or not, where there is no transfer of the assets from which the income arises, be chargeable to income-tax as the income of the transferor and shall be included in his total income.

### Issue

The existing provisions of section 60 provide that income arising to a person under a transfer, where the asset from which the income arises is not transferred, shall be included in the total income of the transferor. The clubbing provisions are intended to check the abuse whereby the transactions are undertaken to split income with object of avoiding due payment of taxes.

Most of the philanthropic activities in India are currently focused towards enhancing health care, reducing extreme poverty, expanding educational opportunities etc. Achieving this goal requires a substantial and steady flow of funds.

Many wealth creators/ promoters especially of large listed companies need to retain control from a strategic business perspective. Various stakeholders such as Institutional investors, shareholders, JV partners etc. expect oversight and control from individual promoters. In such a situation, the only way for achieving philanthropy is that while the promoter does not part with shares (i.e. voting rights), the economic benefits arising from the shareholding i.e. dividends/ capital gains can be renounced towards philanthropy. Similarly, there can be assignment of economic benefits like interest etc. flowing through other financial instruments/ units.

However, under the existing provisions of Section 60 this renouncement of economic interest towards philanthropy, without transfer of shares/financial instrument would result in dividend/ interest income being taxed in the hands of the person renouncing the income.

The clubbing of income in hands of the renouncer results in high tax incidence thereby, leaving lower funds available for philanthropy in the hands of the charity, whereas clearly the right of disposal and use of income is with charity.

Considering the above, if the philanthropist/ donor intends to renounce their economic rights in the shareholding or assign economic benefits to a registered trust or institution for charitable purpose, a facilitating mechanism needs to be put in place whereby the benefits can be passed on directly to the charitable institution. This would ensure fund flow for charitable purposes without diluting any of the stated policy objectives of the Government.

**Suggestion**

It is suggested that section 60 may be amended to provide that the provision would not apply in respect of any transfer of income by way of written renouncement by any person in favour of a charitable institution having medical relief, educational purposes or yoga, etc. as its approved object/the focus area of its activity and which is registered under section 12AB of the Act, provided that such an assignment of income is for a period of not less than 5 years

This limited exception, with focused utilization and identified recipient (which is a well monitored and controlled entity under the Act) would not in any way dilute the primary objective of the Section 60 (to address abusive / fraudulent splitting of income). Instead, it will ensure smooth optimal and assured flow of funds for the charitable activities.

The suggested amendment in section 60 is as under:

"*Transfer of income where there is no transfer of assets.*

*All income arising to any person by virtue of a transfer whether revocable or not and whether effected before or after the commencement of this Act shall, where there is no transfer of the assets from which the income arises, be chargeable to income-tax as the income of the transferor and shall be included in his total income;*

*Provided that nothing contained in this section shall apply to a transfer by any person of his right to receive an income to a trust or an institution registered under section 12AB for a charitable purpose defined in section 2(15), if the following conditions are satisfied, namely:-*

*(i) the transfer is by way of an instrument in writing and;*

*(ii) the assignment of income is for a minimum period of five years.*

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

# 3

# AGGREGATION OF INCOME AND SET OFF AND CARRY FORWARD OF LOSS

## 38. Sections 24, 71(3A) and 115BAC(1A) – Non-permissibility of interest deduction upto Rs.2 lakh and restriction of set off of loss from house property against income under other heads and restriction of carry forward of such loss under the default tax regime – Need for relaxation of restrictions

### Provision of Law

As per section 71, loss from house property can be set-off against income any other head of income only to the extent of Rs.2 lakh. The unabsorbed loss from house property has to be carried forward for set-off against income from house property upto subsequent 8 assessment years.

In case of individuals paying tax under the default tax regime, deduction of interest upto Rs.2 lakh in case of interest on loan borrowed for purchase/construction of self-occupied property is not allowed. Also, even in case of let out property, though there is no restriction on interest deduction u/s 24, the loss, if any, from house property can neither be set-off against income from any other head nor be carried forward.

### Issue

Individuals belonging to middle income group generally purchase property by obtaining loan from the banks. The amount of interest paid is always higher than the rental income earned against such property resulting in a loss from house property. However, non-permissibility of interest deduction u/s 24 for self-occupied property has adversely affected salaried persons who have borrowed money to acquire a house. Also, for let-out property, even though there is no restriction on interest deduction u/s 24, loss under the head "income from house property" cannot be set-off against income under any other head; nor can it be carried forward to the next year for set-off against income, if any, from house property.

**Suggestion**

It is, therefore suggested to permit interest deduction upto Rs.2 lakh under the default tax regime u/s 115BAC(1A) also. Also, set-off of loss from house property against income under other heads should be permitted under the default tax regime. If there is no income under any other head, then the loss must be permitted to be carried forward for set-off against income from house property in the next year; such carry forward must be permitted for 8 years.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 39. Section 72A - Carry forward of losses in case of amalgamation or demerger – Definition of "industrial undertaking" be amplified to include the business of providing all services

### Provision of Law

As per section 72A(7)(aa), industrial undertaking" means any undertaking which is engaged in—

(i) the manufacture or processing of goods; or

(ii) the manufacture of computer software; or

(iii) the business of generation or distribution of electricity or any other form of power; or

(iiia) the business of providing telecommunication services, whether basic or cellular, including radio paging, domestic satellite service, network of trunking, broadband network and internet services; or

(iv) mining; or

(v) the construction of ships, aircrafts or rail systems;

### Issue

Currently, all industrial undertakings in the Manufacturing, Software, Electricity, Telecom, etc. sectors are allowed to carry forward losses in case of amalgamation/demerger. Service industry undertakings in general are not allowed such carry forward with the exception of an undertaking engaged in the business of providing telecommunication services, whether basic or cellular, including radio paging, domestic satellite service, network of trunking, broadband network and internet services.

Media and Entertainment Industry requires huge investment in digitization, technology set up and distribution network. As per the Notification issued by the Govt. in 2004, Broadcasting and Cable Services are a part of Telecommunication Services. Consolidation of media industry will help in rapid growth and generation of substantial employment opportunities and faster digitization.

### Suggestion

It is suggested to amend section 72A(7)(aa) defining "industrial undertaking" to include other services also within its ambit.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 40. Section 79 – Conditions for carry forward and set off of loss in case of eligible start-ups - Suggestion for relaxation of the conditions

### (a) Relaxation of condition for carry forward and set off

**Provision of Law**

Section 79(1) reads as follows -

"*Notwithstanding anything contained in this Chapter, where a change in shareholding has taken place during the previous year in the case of a company, not being a company in which the public are substantially interested, no loss incurred in any year prior to the previous year shall be carried forward and set off against the income of the previous year, unless on the last day of the previous year, the shares of the company carrying not less than fifty-one per cent of the voting power were beneficially held by persons who beneficially held shares of the company carrying not less than fifty-one per cent of the voting power on the last day of the year or years in which the loss was incurred.*

*Provided that even if the said condition is not satisfied in case of an eligible start-up as referred to in section 80-IAC, the loss incurred in any year prior to the previous year shall be allowed to be carried forward and set off against the income of the previous year if all the shareholders of such company who held shares carrying voting power on the last day of the year or years in which the loss was incurred, continue to hold those shares on the last day of such previous year and such loss has been incurred during the period of ten years beginning from the year in which such company is incorporated.*"

**Issue**

Section 79(1) contains restrictions on carry forward of losses in case of substantial change in shareholding of the Indian company, not being a company in which the public are substantially interested. As per the said section, for set-off of loss, the shares of the company carrying not less than 51% of the voting power should be beneficially held by persons who beneficially held shares of the company carrying not less than 51% of the voting power on the last day of the year or years in which the loss was incurred

The Government, in pursuance of the start-up action plan and facilitating ease of doing business, introduced a beneficial regime for start-up to carry forward and set off losses. Accordingly, the proviso to section 79(1) provides that where a change in shareholding has taken place in a previous year in the case of a company, not being a company in which the public are substantially interested and being an eligible start-up as referred to in section 80-IAC of the Act, loss shall be carried forward and set off against the income of the previous year, if all the shareholders of such company which held shares carrying voting power

on the last day of the year or years in which the loss was incurred, being the loss incurred during the period of 10 years beginning from the year in which such company is incorporated, continue to hold those shares on the last day of such previous year.

The condition of continuing to hold all shares appears to be applicable not only to the initial promoters but also all persons investing subsequently in the startup, which may cause genuine practical hardship. This may also be practically difficult for the start-up company to achieve since PE investors generally look at time frame of 3 to 5 years to exit at a higher price. The exit may happen either through secondary sale in subsequent round of PE funding or through IPO. Any such exit will trigger section 79 limitation for the start-up company.

**Suggestion**

It is, therefore, suggested that the condition of continuous holding of the promoters/investors (being persons holding shares in the year of loss) be relaxed and inter-se transfers between such shareholders be permitted.

## (b) Section 79(2)(c) - Relief for a company where change in shareholding takes place pursuant to a resolution plan approved under the IBC - Relief also to be extended where there is change in shareholding of subsidiaries pursuant to resolution plan.

**Provision of Law**

Section 79 restricts the carry forward and set off of losses in the hands of a closely held company, if the shares carrying more than 51% of voting power of such company are not beneficially held by persons who beneficially held such shares on the last day of the previous year in which such loss was incurred.

**Issue**

In general, implementation of resolution plan in respect of a company undergoing resolution process may involve either issue of additional shares or other restructuring exercise resulting in change in the shareholding of such company beyond the permissible limit u/s 79.

In addition thereto, the company may also be required to hive off its investments in subsidiaries by selling its stake to interested investors. This may result in change in shareholding of the subsidiaries triggering consequences u/s 79 of the Income-tax Act, 1961 in the hands of subsidiaries as well. Hence, this may discourage the interested acquirers/bidders from making investments in loss making subsidiaries and also in offering higher bids.

However, section 79(2) provides for certain exceptions from applicability of this condition. Clause (c) thereof states that section 79 will not apply to companies, where the change in the shareholding is pursuant to implementation of a resolution plan approved Insolvency and Bankruptcy Code, 2016. This benefit is to be provided after an opportunity of being heard is given to the jurisdictional Commissioner or Principal Commissioner.

In terms of the clause (c) to section 79(2), carry forward and set off of losses of a company undergoing insolvency resolution process as well as its subsidiaries will not be impacted by section 79, if the change in shareholding takes place pursuant to a resolution plan approved under IBC, 2016.

While such be the case, it is likely that NCLT will not hear Principal Commissioner/Commissioner holding jurisdiction over the subsidiaries. Hence, the reference to an opportunity of being heard to be given to the Principal Commissioner/Commissioner may be interpreted to relate only to the company which is undergoing a resolution process under IBC.

**Suggestion**

It is suggested that section 79(2)(c) be amended to clarify that it applies both to the company undergoing resolution process as well as its subsidiaries. The provision may be modified as follows:

*"Nothing contained in sub-section (1) shall apply to a company as well as its subsidiary where a change in the shareholding takes place in a previous year pursuant to a resolution plan approved under the Insolvency and Bankruptcy Code, 2016, after affording a reasonable opportunity of being heard to the jurisdictional Principal Commissioner or Commissioner holding jurisdiction over the applicant".*

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

# 4

# TAXATION OF COMPANIES

## 41. Section 115BAA – Special tax regime for companies - Deduction u/s 80G to be allowed while computing total income under these special tax regimes

### Provision of Law

Section 115BAA contains the special tax regime for companies, wherein they are eligible for concessional tax rate of 22%, subject to satisfaction of certain conditions, including non-availability of deductions under Chapter VI-A, except sections 80JJAA and 80M.

### Issue

Deduction under, *inter alia*, section 80G is not allowed while computing total income where the companies have opted for beneficial provisions of section 115BAA and subject to a concessional tax rate thereunder.

It is noteworthy that deduction u/s 80JJAA is allowed under the special regime to generate more employment. Likewise, donations for charitable purpose may be promoted by the Government for wellbeing of society at large. Deduction for donation made would motivate the donor to donate towards charitable activities.

### Suggestion

It is suggested to include donations qualifying for deduction u/s section 80G for companies opting for tax under the provisions of section 115BAA.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 42. Section 115JB -Minimum Alternate tax – Provision for bad and doubtful debts and amounts set aside for reserve created in accordance with the provisions of section 36(1)(viii) to be allowed while computing book profit of banking companies

### Provision of Law

As per clause (i) of *Explanation 1* to section 115JB, the amount or amounts set aside for provision for diminution in value of any asset has to be added back for computation of "book profit". Likewise, as per clause (b) thereof, the amount carried to any reserves, by whatever name called, other than reserve specified under section 33AC, has to be added back.

### Issue

In case of banking companies, the applicability of this clause may be reconsidered. This is because of the fact that, in computation of business income under normal provisions, deduction in respect of provision for bad debts is allowed under section 36(1)(viia) subject to the limit specified therein. If provision for bad debts is allowed as deduction in computation of business income under normal provisions, there does not appear to be any cogent reason for adding back the same in computation of "book profit" under section 115JB. Similarly, any special reserve created in accordance with the provisions of section 36(1)(viii) should not be required to be added in computation of book profit under section 115JB.

### Suggestion

It is suggested that clause (b) and (i) of Explanation 1 to section 115JB may be amended as follows-

*"(b) the amounts carried to any reserves, by whatever name called [other than a reserve specified under section 33AC and a reserve created and allowed in accordance with the provisions of section 36(1)(viii)]*

*(i) the amount or amounts set aside as provision for diminution in the value of any asset (other than provision for bad and doubtful debts allowed as a deduction under section 36(1)(viia)"*

***(SUGGESTION FOR REDUCING/MINIMISING LITIGATION)***

## 43. Clause (iih) in *Explanation 1* to section 115JB- Downward adjustment of aggregate brought forward losses and depreciation u/s 115JB – Clarification as to whether the same has to be as per books of account & Extension of benefit to a company into which the defaulting company merges consequent to resolution plan

### Provision of Law

As per clause (iih) of *Explanation 1* to section 115JB, while computing book profit u/s 115JB, deduction is allowed for aggregate of book profit and unabsorbed depreciation in case of companies in respect of which an application for initiating resolution process has been accepted by the adjudicating authority.

### Issues

(i) It is not clear as to whether aggregate of losses and depreciation as per books is to be considered for deduction or whether aggregate of losses and depreciation as computed for tax purposes is to be considered for downward adjustment from book profit.

(ii) The phrase "as per books of account" being specifically mentioned in clause (iii) relevant for other companies whereas the same is not mentioned in clause (iih). The scheme of MAT is linked to book profit. The legislative intent also appears to be to refer to the amounts as per books of account. However, the difference in language used in clause (iih) and clause (iii) creates an element of doubt.

(iii) Re-organisation by way of merger of distressed company is one of the known forms of reorganising distressed companies against whom proceeding under IBC has been initiated. There is a concern that the benefit u/s 115JB has been extended merely to the defaulting/distressed company against whom the application for resolution plan has been admitted and thus may not extend to the company into which the defaulting company may merge pursuant to the implementation of the resolution plan.

**Suggestion**

It is suggested that suitable clarification may be inserted in section 115JB to clarify that the brought forward losses and unabsorbed depreciation for this purpose should be considered as per books of account. It may be provided that the aggregate of the brought forward losses and unabsorbed depreciation as at the end of the year preceding the year in which application is admitted may be allowed to be reduced.

This benefit may be extended to the company with which the distressed company merges consequent to the resolution plan.

Also, since the concessional tax regime under section 115BAA has been introduced to encourage companies to opt for the same, a sunset clause may be introduced for applicability of MAT provisions.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 44. Section 2(19AA) – Definition of Demerger – Scope of definition may be expanded to include spin-offs – Consequential amendments to be made in section 2(22)(e), section 2(41A), section 47 and section 56(2)(x)

### Provision of Law

As per section 2(19AA), "*demerger", in relation to companies, means the transfer, pursuant to a scheme of arrangement under sections 391 to 394 of the Companies Act, 1956), by a demerged company of its one or more undertakings to any resulting company in such a manner that—*

*(i) all the property of the undertaking, being transferred by the demerged company, immediately before the demerger, becomes the property of the resulting company by virtue of the demerger;*

*(ii) all the liabilities relatable to the undertaking, being transferred by the demerged company, immediately before the demerger, become the liabilities of the resulting company by virtue of the demerger;*

*(iii) the property and the liabilities of the undertaking or undertakings being transferred by the demerged company are transferred at values appearing in its books of account immediately before the demerger:*

*(iv) the resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis except where the resulting company itself is a shareholder of the demerged company;*

*(v) the shareholders holding not less than three-fourths in value of the shares in the demerged company (other than shares already held therein immediately before the demerger, or by a nominee for, the resulting company or, its subsidiary) become shareholders of the resulting company or companies by virtue of the demerger, otherwise than as a result of the acquisition of the property or assets of the demerged company or any undertaking thereof by the resulting company;*

*(vi) the transfer of the undertaking is on a going concern basis;*

*(vii) the demerger is in accordance with the conditions, if any, notified under sub-section (5) of section 72A by the Central Government in this behalf.*

### Issue

The existing provisions of Section 2(19AA) define "demerger" and if the demerger carried out as part of corporate restructuring satisfies the condition, then, tax neutrality is ensured both for the companies involved and shareholders. The tax neutrality is in respect of both capital gains and the dividend taxation.

Listed companies generally carry-on different businesses which are distinct and diverse from each other through the subsidiaries given the applicable regulatory

environment or different risk profile or due to different set of investors for different business segments.

At a certain stage of growth or development of business of that subsidiary, a natural preference would be to list that subsidiary to secure its future investments and growth or to benefit from improved access of capital, an increased global profile and for greater access to liquidity or to give exit to the private equity investors etc. Listing of a company is always beneficial to the company, to the investor, and to the public at large. It also adds to the economic activities in the country. An initial public offer (IPO) is one of the ways a company can get listed. To list a company through an IPO process is a time consuming and a high-cost event. One of the best international practices for simple and easier listing of a company could be - a listed company distributes its shareholding in a subsidiary to its shareholders. This is form of corporate divesture and is a category of demerger known in commercial world as "Spin-off". After the distribution is completed, the spun off company is no longer a subsidiary of the parent and the parent's shareholders hold not only the parent's stock but also the subsidiary's stock. As the parent is publicly held company, the subsidiary also becomes a publicly held company subject to necessary enabling provisions.

The Income-tax Act, 1961 recognizes the importance of business reorganisation undertaken by the groups for various commercial reasons. In order to facilitate these reorganisations, the Act provides for tax neutrality for the same. Under the existing provisions of the Act, tax neutrality has been provided for both amalgamation and demerger of companies subject to certain conditions and also to the intra group transfer of assets between subsidiary and holding company.

Presently, the Act provides for tax neutrality only for a specific kind of demerger where a business undertaking can be demerged into a separate resulting company. The corporate divestiture in form of spin-off is not presently covered under the tax neutrality provisions. If the parent company distributes shares of subsidiary company, the said transaction would be considered as dividend distributed by parent company to its shareholders and accordingly, fair market value of shares of the subsidiary company received by the shareholder would be taxed as dividend income in the hands of shareholders.

However, considering the commercial reasons and in line with the tax neutrality provided to corporate reorganisation in form of amalgamation and demerger, there is need for providing tax neutrality for corporate divestiture by way of spin off subject to certain conditions. Providing tax neutrality for spin-off in case of a listed company would only result in deferral of taxes for a limited period. If there is no tax neutrality, the tax on dividend gets charged up front. However, if tax neutrality is provided, the shareholder would pay capital gain tax subsequently as and when the shares of either company are sold by it and also continue to pay dividend tax on any dividends declared by either of the company post spin-off.

The global practice also indicates that many countries have provided tax neutrality to spin-off transactions as part of their tax regime related to corporate reorganisation. The broad contours of policy followed by some advanced economies indicates that basic emphasis of the countries, while giving tax neutrality to spin-off transactions, is to impose conditions. Certain conditions relating to control prior to spin-off, distribution of sufficient level of shareholding and active business being the subject matter of transaction are provided for to ensure that abuse of the provisions are avoided.

Under the existing provisions of the Act relating to tax neutrality to business reorganisation also, certain conditions have been imposed before neutrality is granted. The tax neutrality can be provided for spin-off transactions on the lines of existing provision for demerger of the company. Further, initially the benefit may be restricted to spin-off being undertaken by listed company. This will ensure that there is no risk of any abuse of the benefits.

**Suggestion**

It is suggested that section 2(19AA) may be amended to include in the definition of demerger, the corporate divestiture in form of spin-off under which a parent company transfers its shareholding in a subsidiary to its shareholders. Initially, such an inclusion be made only in respect of parent company being a listed company.

Further, to ensure that distribution by the holding company to its shareholders of the shares of the subsidiary is not taxable as dividend, an exclusion also needs to be made for such distribution in case of Spin off from definition of dividend under section 2(22).

Consequential amendments may be made in section 2(19AAA), section 2(41A), section 47 and section 56(2)(x).

Draft of suggested amendment(s) is given below:

(i) Amendment in the definition of demerger

The provisions of section 2(19AA) may be amended as under –

*2(19AA). "demerger", in relation to companies, means the transfer, pursuant to a scheme of arrangement under sections 391 to 394 of the Companies Act, 1956 (1 of 1956), by a demerged company of -*

*(a) its one or more undertakings to any resulting company in such a manner that-*

*----------*

*(b) specified shares held by it to all its shareholders in proportion of the paid up value of their shareholding in the demerged company;*

*……..*

*Explanation 7. For the purposes of this clause, "specified shares" means whole of the share capital as is held by demerged company in a subsidiary (being an Indian company), where the demerged company, being a company the shares (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in profits) of which are on the day of transfer of the specified shares listed on a recognized stock exchange in India.*

(ii) Amendment in the definition of demerged company

The provisions of section 2(19AAA) may be amended as under –

*2(19AAA) "demerged company" means the company whose undertaking or specified shares held by it is transferred, pursuant to demerger, to a resulting company or the shareholders of the demerged company as the case may be;*

(iii) Amendment in the definition of dividend

The provisions of section 2(22) may be amended as under –

*2(22) "dividend" includes—*

*----------*

*but "dividend" does not include—*

*-------*

(v) any distribution of shares pursuant to a demerger by the resulting company to the shareholders of the demerged company (whether or not there is a reduction of capital in the demerged company);

(vi) any distribution of specified shares referred to in Explanation 7 to clause (19AA) of section 2 under a scheme of demerger by the demerged company to the shareholders of the demerged company.

(iv) Amendment in the definition of resulting company

The provisions of section 2(41A) may be amended as under –

*2(41A)."resulting company" means –*

*(a) one or more companies (including a wholly owned subsidiary thereof) to which the undertaking of the demerged company is transferred in a demerger and, the resulting company in consideration of such transfer of undertaking, issues shares to the shareholders of the demerged company and includes any authority or body or local authority or public sector company or a company established, constituted or formed as a result of demerger; or*

*(b) the subsidiary company being an Indian company), the specified shares of which are transferred in a demerger by the demerged company to shareholders of the demerged company.*

(E) The provisions of section 47 may be amended as under –

47. Nothing contained in section 45 shall apply to the following transfers :—

*----------*

*(vie) any transfer of specified shares by the demerged company to its shareholders, in a scheme of demerger;*

(F) The provisions of section 56(2)(x) may be amended as under –

*56(2)(x)-----*

*Provided that this clause shall not apply to any sum of money or any property received—*

*(IX) by way of transaction not regarded as transfer under clause (i) or clause (iv) or clause (v) or clause (vi) or clause (via) or clause (viaa) or clause (vib) or clause (vic) or clause (vica) or clause (vicb) or clause (vid) or clause (vie) or clause (vii) or clause (viiac) or clause (viiad) or clause (viiae) or clause (viiaf)] of section 47; or*

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 45. Section 2(19AA) – Definition of Demerger – Clarification as to whether the gross value or net value of assets has to be taken for apportionment of general borrowings

**Provision of Law**

Section 2(19AA) provides for the definition and conditions under which a demerger involving transfer of an undertaking from a company (demerged company) to another company (resulting company) shall be tax neutral. One of the conditions mentioned in sub-clause (ii) of the said clause is that all liabilities related to the undertaking immediately before demerger become the liabilities of the resulting company.

Further, *Explanation 2* to the said clause details the liabilities to be considered for sub-clause (ii) i.e., to be transferred to the resulting company. The said *Explanation* is as under:-

"*Explanation 2 - For the purposes of this clause, the liabilities referred to in sub-clause (ii), shall include—*

*(a) the liabilities which arise out of the activities or operations of the undertaking;*

*(b) the specific loans or borrowings (including debentures) raised, incurred and utilised solely for the activities or operations of the undertaking; and*

*(c) in cases, other than those referred to in clause (a) or clause (b), so much of the amounts of general or multipurpose borrowings, if any, of the demerged company as stand in the same proportion which the value of the assets transferred in a demerger bears to the total value of the assets of such demerged company immediately before the demerger*."

**Issue**

There is lack of clarity in respect of the apportionment of general or multipurpose borrowings. It is not clear as to whether for apportionment, only gross value of assets has to be taken or the net value after reducing specific liabilities related to the assets has to be considered. This at times may lead to avoidable controversies and litigation.

It is, therefore, suggested that it be clarified as to whether gross assets shall be taken in computation of apportionment or the net assets (i.e., assets as reduced by specific liability related to an asset) shall be taken. The same clarification would apply to both the numerator and the denominator of the apportionment formula.

**Suggestion**

It is suggested that the provisions of clause (19AA) of section 2 be amended to clarify that for the purposes of clause (c) of *Explanation 2*, whether it is gross value of assets or net assets (after excluding specific liabilities corresponding to the assets) which is to be taken.

***(SUGGESTION FOR REDUCING/MINIMIZING LITIGATION)***

## 46. Section 2(41A) - Definition of resulting company – Scope to expanded to include holding company, where the resulting company is a wholly owned subsidiary

### Provision of Law

Section 2(41A) provides definition of the resulting company in context of demerger which is defined under section 2(19AA). As per section 2(19AA)(iv), one of the condition for tax neutrality of the demerger under the Act is that "the resulting company issues, in consideration of demerger, its shares to the shareholders of the demerged company". Therefore, it is resulting company which must issue its shares.

Section 2(41A) containing the definition of "resulting company" provides as follows -

*"resulting company" means one or more companies (including a wholly owned subsidiary thereof) to which the undertaking of the demerged company is transferred in a demerger and, the resulting company in consideration of such transfer of undertaking, issue shares to the shareholders of the demerged company and includes any authority or body or local authority or public sector company or a company established, constituted or formed as a result of demerger*

### Issue

From the above definition, the inclusion of the phrase in the bracketed portion "(including a wholly owned subsidiary thereof)" conveys the meaning that where an undertaking is demerged to a wholly owned subsidiary, then, both holding company and the wholly owned subsidiary are resulting company, apart from the holding company being the demerged company. The implication is, therefore, that in a demerger, a holding company can issue its shares to its shareholders instead of the wholly owned subsidiary (to which the undertaking has been transferred) issuing its shares to the shareholders of the holding company.

This lack of clarity as to whether an option exists that either the wholly owned subsidiary or its holding company can issue its shares as a consideration for the demerger has led to avoidable controversy and potential litigation.

The intention of the policymakers may be clearly brought out by mentioning that the shares of either the holding company or the wholly owned subsidiary can be issued in consideration of demerger.

### Suggestion

It is suggested that sections 2(19AA)(iv) and 2(41A) may be amended to clarify that where the demerger of an undertaking is to a company which is wholly owned subsidiary, then, both the wholly owned subsidiary company to which the undertaking is transferred and holding company shall be treated as resulting company for purposes of demerger related provisions particularly in the context of issue of shares as consideration of demerger.

## 47. Section 10 – Exemption for dividend from companies under certain circumstances

### Provision of law

Section 10 provides for exclusion of income specified under different clauses thereunder in computing the total income of a previous year of any person. Upto 31.3.2020, companies were subject to dividend distribution tax under section 115-O, consequent to which dividend was exempt u/s 10(34) in the hands of shareholders. However, w.e.f. 1.4.2020, dividend distribution tax is not levied, and hence the exemption u/s 10(34) was withdrawn.

### Issue

Under the existing provisions relating to taxation of dividend, the dividend income is taxable in the hands of a shareholder under the head "Income from other sources". Further, no expenses other than interest (limited to 20% of the dividend) is allowed while computing income chargeable to tax.

Domestic company is provided deduction under section 80M in respect of inter-corporate dividends received. The amount of deduction is limited to the amount which has been further distributed by the company before due date of filing of return u/s 139(1) for the relevant assessment year.

In addition, the dividend income is also liable to tax under Minimum Alternate Tax (MAT). There is no relief from cascading effect of taxation under MAT even if the company has distributed dividends further to its shareholders.

The deduction under section 80M being conditional upon further distribution of the dividend induces a distortion by creating high tax cost for reinvestment of funds received by the recipient entity. The forced capital outflow from the business due to tax distortion is not a desirable policy outcome in cases of genuine business activities needing funds at competitive costs.

The reinvestment of internal generation within a group suffers high tax cost. Accordingly, the funds are forced to move out of the productive business cycle. Absence of any relief from MAT liability on dividend income irrespective of whether any retention of dividend has taken place at inter-corporate level or not compounds the problem of high tax cost significantly.

It is a known fact that, due to regulatory reasons, a company is required to set up subsidiaries and special purpose vehicles. Similarly, engagement in diverse businesses at times necessitates creation of multiple entities. Presence of different subsidiaries in a corporate structure is, therefore, an outcome of both regulatory and genuine commercial requirement.

If the tax induced distortions in allocation of capital cannot be eliminated, then, the need of its reduction in a targeted manner is the most desirable policy response. It

is on this fundamental basis that international best practice is to have "participation exemption" relief widely defined to avoid economic double taxation on inter-corporate dividends from shareholdings or participations. This ensures productive utilization of resources within a group without tax leakage.

The international practice indicates that, in majority of countries, the inter-corporate dividend is either exempt or a participation exemption is provided based on certain conditions. The general principle followed is of granting deduction in respect of dividends received from other companies wherein the recipient company shareholding exceeds certain minimum threshold. It may not be out of place to mention that the requirement of further distribution, within limited time span, by the recipient company to avail deduction in respect of inter-corporate dividends under the Act is a concept not being followed in most of the countries. Further, absence of any relief while computing tax liability under MAT results in continued undesirable cascading effect of taxation.

The condition of further distribution under section 80M apparently is with the objective to prevent permanent deferral of taxes on dividends through utilization of interposed corporate entities. In case of private companies where the identity of shareholder and the company merges from a practical point of view due to lack of regulations and absence of governance norms, the indefinite deferral of taxes on dividends may be a reality that needs to be addressed.

However, at the same time, **there is a need to have differentiated policy response in case of companies in which public are substantially interested vis-à-vis closely held companies.** It is undeniable fact that companies whose shares are listed on the recognized stock exchange and their subsidiaries are working under a stringent regulatory regime enforced by market regulators like SEBI and the Ministry of Corporate Affairs which ensures transparency and good governance. The fear of misuse contemplated in a closely held corporate structure may not be there in a structure involving companies in which public are substantially interested. Further, listed companies do follow a pattern of dividend distribution and having public shareholding ensures its compliance.

The merit of differential regime for companies in which public are substantially interested has been well recognized in the various provisions, particularly anti-abuse provisions, in the Act as enumerated below:

1. Exception from applicability of deemed dividend provisions under section 2(22)(e),
2. Exception from applicability of anti-abuse provisions of section 56(2)(viib) for companies in which public are substantially interested, and
3. Exception from the widened scope of increased burden under the second proviso to section 68.

Considering the regulatory and governance oversight, the risk of indefinite deferral of taxation of dividends in case of listed companies and its subsidiaries is not real.

Accordingly, there is an urgent need to provide a special regime in respect of taxation of inter-corporate dividends in cases of companies in which public are substantially interested particularly for listed companies and its subsidiaries.

The amendment of the Act be considered in order to include a special dispensation in respect of inter-corporate dividends received by a listed company and its subsidiaries from domestic companies and InVITs which are part of the same group.

**Suggestion**

It is suggested that section 10 be amended to provide that a domestic company whose shares are listed on a recognized stock exchange or its subsidiaries be granted exemption in respect of any income by way of dividend received from a domestic company which is part of the same group. The same exemption shall apply to any dividend received from an InVIT set up by the listed company or its subsidiaries as sponsor. This same exemption be provided under MAT by making suitable amendments to section 115JB.

A draft of suggested amendment in section 10 is placed below:

*"(34AA) any income by way of dividends received by a domestic company from other domestic company or a business trust where such domestic company, the other domestic company or the business trust belong to the same specified group;*

*Explanation: For the purposes of this clause, the expression "specified group "means a group of entities that includes,-*

*(a) a company, shares (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in profits) of which were as on the last day of the relevant previous year listed on a recognized stock exchange in India;*

*(b) any subsidiary company of a company falling under this Explanation;*

*(c) a business trust referred to in sub-clause (i) of clause (13A) of section 2 in respect of which a company falling under this clause is a sponsor as defined under clause (zz) of Regulation 2 of Securities and Exchange Board of India (Infrastructure Investment Trusts) Regulations, 2014;"*

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

# 5

# TAXATION OF FIRMS & LIMITED LIABILITY PARTNERSHIPS

## 48. Chapter XII – Special Tax Regimes for individuals/HUFs/AOPs/ BOIs/Companies/Co-operative Societies – Need for introduction of special tax regime for firms and LLPs

**Issue**

Special tax regime has been introduced for individuals/HUFs/AOPs/BOIs, companies and co-operative societies. Under the special tax regime, the assessees pay tax computed at a lower rate on total income computed without specified deductions. For individuals/HUFs/AOPs/BOIs, the special tax regime u/s 115BAC(1A) is the default tax regime. Companies and co-operative societies, however, have to opt for the special tax regime contained in section 115BAA and 115BAD/115BAE, respectively. At present, there is no special tax regime for firms and LLPs.

**Suggestion**

It is suggested that special tax regime be introduced which firms and LLPs can opt for and pay tax at concessional rate@22% (*plus* surcharge@10% plus cess@4%) on total income computed without specified deductions and exemptions.

Simplified return forms can be prescribed for such firms/LLPs/companies/co-operative societies opting for special tax regime.

***(SUGGESTION FOR REDUCING COMPLIANCE BURDEN)***

# 6

# TAXATION OF INDIVIDUALS

## 49. Section 115BAC - Default tax regime for individuals/HUFs/AOP/BOI/ Artificial Juridical Persons in which deductions under Chapter VI-A are not allowed except section 80JJAA - Mediclaim premium/expenditure to be allowed u/s 80D

**Provision of Law**

The default tax regime of individuals/HUF/AOP/BOI/Artificial Judicial Persons is provided under section 115BAC from A.Y. 2024-25, wherein total income computed without any deduction under, *inter alia*, Chapter VI-A (except deduction under section 80JJAA) is subject to tax at concessional rates specified thereunder.

**Issue**

It is beneficial only for tax payers who do not invest and/or save for tax benefits. It would put more money in the hands of such tax payers. However, certain concerns enumerated below merit consideration.

Under section 80D, premium paid towards medical insurance for family members is allowed as deduction from gross total income. Till the time subsidized medical/healthcare facilities are available to all tax payers, it may be considered that at least medical insurance premium paid for family members allowable as deduction u/s 80D be allowed u/s 115BAC. It would continue to encourage all tax payers including the taxpayers paying tax under the default tax regime to keep their mediclaim policy alive to secure the health of the family members.

**Suggestion**

It is suggested that at least deduction u/s 80D i.e. premium paid for keeping medical insurance policy for self and family members and/or medical expenditure incurred be allowed as a deduction even for assessees opting for section 115BAC in order encourage such tax payers to continue their mediclaim policy by paying premium, considering limited affordable healthcare facilities in the country.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 50. Section 115BAC - Default tax regime for individuals/HUFs/AOP/BOI/ Artificial Juridical Persons in which deductions under Chapter VI-A are not allowed except section 80JJAA - Separate provision for deduction of expenses relating to education of girl child both under the default tax regime and optional tax regime

**Provision of law**

The default tax regime of individuals/HUF/AOP/BOI/Artificial Judicial Persons is provided under section 115BAC from A.Y. 2024-25, wherein total income computed without any deduction under, *inter alia*, Chapter VI-A (except deduction under section 80JJAA) is subject to tax at concessional rates specified thereunder.

Under section 80C, deduction is allowed in respect of payment of life insurance premium, repayment of housing loan, investment in PPF, contribution to RPF, tuition fees for education of children and contribution to Sukanya Samriddhi Scheme etc. However, this deduction is not allowable under section 115BAC.

**Issue**

The government's emphasis on promoting the education of girl children is commendable. However, the current tax provisions do not adequately allow expenditure towards their education. Presently, only tuition fees paid to educational institutions and contribution to Sukanya Samriddhi Scheme are eligible for deduction u/s 80C. Section 80C is available only where an individual opts out of the default tax regime. Also, many investments/payments are covered within the scope of deduction u/s 80C, namely, payment of life insurance premium, repayment of housing loan, investment in PPF, contribution to RPF, etc. There is a need for a separate and enhanced deduction specifically for expenses incurred on the education of girl children, both under the default tax regime and the optional tax regime.

**Suggestion**

It is suggested that a separate deduction be introduced under Chapter VIA of the Income-tax Act, 1961 to allow the expenditure on the education of girl children both under the default tax regime under section 115BAC and under the optional tax regime. Furthermore, the deduction should cover a broader spectrum of educational expenses (including expenses for pursuing professional accounting education) beyond just tuition fees and contribution to Sukanya Samriddhi Scheme.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 51. Section 115BAC – Default tax regime of individuals – Introduction of option for Joint Taxation System of married couples with increased basic exemption limit and rationalized tax slabs and surcharge slabs and provision for filing of joint return of income

**Provision of Law**

Currently, under the Income-tax Act, 1961, different tax slabs are provided for, inter alia, individuals. The rates increase progressively as the income increases. Section 115BAC is the default tax regime for, inter alia, an individual.

The tax rates for an individual under the default tax regime u/s 115BAC is as follows –

| S. No. | Total Income | Rate of tax |
|---|---|---|
| 1. | Upto Rs.3,00,000 | Nil |
| 2. | From Rs.3,00,001 to Rs.7,00,000 | 5% |
| 3. | From Rs.7,00,001 to Rs.10,00,000 | 10% |
| 4. | From Rs.10,00,001 to Rs.12,00,000 | 15% |
| 5. | From Rs.12,00,001 to Rs.15,00,000 | 20% |
| 6. | Above Rs.15,00,000 | 30% |

An individual who exercises the option to opt out of the default regime under section 115BAC, has to pay tax as per normal provisions of the Act. To pay tax as per normal provisions of the Act, the rates of tax are prescribed by the Annual Finance Act of the year.

For an individual, the basic exemption limit is Rs.2,50,000. No tax is payable by an individual with total income of up to Rs.2,50,000. An individual whose total income is more than Rs.2,50,000 but less than Rs.5,00,000, has to pay tax on their total income in excess of Rs.2,50,000@5%. Total income between Rs.5,00,000 and Rs.10,00,000 attracts tax @20%. The highest rate is 30%, which is attracted in respect of income in excess of Rs.10,00,000.

Individuals are entitled to benefit from these tax slabs, with each member of a family eligible for the basic exemption limit separately. For instance, in a family of four comprising a husband, wife, and two children, each member can avail of the basic exemption limit of Rs.3 lakh separately under the default regime.

**Issue**

In the case of families where both the husband and the wife are earning, they can avail of a separate basic exemption limit of Rs.3 lakh (under default scheme) and Rs.2.50 lakh under the optional scheme as per the normal provisions of the Act. However, in India, a significant number of families rely on a single earning member to support the household. The current basic threshold exemption of Rs.3 lakh/Rs.2.5 lakh, as the case may be, is inadequate considering the prevailing cost of living. Consequently, there may be a tendency for families to explore ways and means to generate income for each family member to take advantage of individual exemption limits.

For example, the husband, wife and their children all are entitled to basic exemption limit of Rs.3 lakh separately under default regime/Rs.2.50 lakh under the optional regime. In a country like India, even today 80% of the families are supported by a single individual. In many households, women and children may not have separate earnings and are supported by a single sole earning male member. In the circumstances, for an average size of a family of four members i.e. husband, wife and two children, the basic threshold exemption of Rs.3 lakh/Rs.2.50 lakh is very low considering the current cost of living. Therefore, it encourages adoption of ways and means to transfer income in hands of other family members.

**Suggestion**

It is suggested to introduce an **option for joint taxation of married couples by filing a joint return of income**. Individuals may be given an option to pay tax under the Joint Taxation Scheme. They can choose to pay tax individually under the present scheme of taxation or opt for joint taxation of self and spouse.

Under the joint taxation scheme, the threshold exemption available may be enhanced by doubling the exemption limit available to individual taxpayers. Also, the tax slabs may be broadened proportionately. Doubling the exemption limit under the Joint Taxation Scheme would better align with the economic realities of such households. Such scheme is already in force in developing countries such as USA.

The rates under the default scheme under section 115BAC in case of joint taxation may be as follows -

| S. No. | Total Income | Rate of tax |
|---|---|---|
| 1. | Upto Rs.6,00,000 | Nil |
| 2. | From Rs.6,00,001 to Rs.14,00,000 | 5% |
| 3. | From Rs.14,00,001 to Rs.20,00,000 | 10% |
| 4. | From Rs.20,00,001 to Rs.24,00,000 | 15% |
| 5. | From Rs.24,00,001 to Rs.30,00,000 | 20% |
| 6. | Above Rs.30,00,000 | 30% |

Correspondingly, the threshold limit for surcharge may be increased to Rs.1 crore. For total income between Rs.1 crore and Rs.2 crore, the rate of surcharge may be 10%; from Rs.2 crore to Rs.4 crore, the rate of surcharge may be 15%; and above Rs.4 crore, the rate of surcharge may be 25%.

In case both husband and wife are salaried employees, the standard deduction u/s 16(ia) should be separately available to them while computing their salary income.

Also, the threshold adjusted total income limit for non-applicability of alternate minimum tax u/s 115JC, which is currently Rs.20 lakhs, may be proportionally increased, in cases where the individual opts out of the default tax regime.

***(SUGGESTION FOR PREVENTION OF TAX AVOIDANCE)***

## 52. Rebate u/s 87A - Income-tax utility not allowing rebate in respect of income-tax on short-term capital gains chargeable u/s 111A and Long-term capital gains chargeable u/s 112 where income is computed under default tax regime u/s 115BAC(1A), though there is no restriction in the Act – Concern to be addressed

### Provision of Law

Rebate u/s 87A is available to a resident individual both under the default tax regime u/s 115BAC(1A) and under the alternative tax regime as per the normal provisions of the Act.

### Issue

Rebate u/s 87A is not allowable in respect of income-tax on capital gains under section 112A, since this section contains a restriction denying such rebate. However, there is no such restriction in respect of short-term capital gains on transfer of equity shares, units of equity-oriented fund and business trust (on which STT is paid) chargeable to tax under section 111A and long-term capital gains chargeable to tax under section 112. The income-tax utility, however, does not provide for rebate u/s 87A in respect of income-tax on short-term capital gains chargeable under section 111A and long-term capital gains chargeable under section 112, where a resident individual pays tax under the default tax regime under section 115BAC(1A). However, such rebate is allowed against short-term capital gains chargeable under section 111A and long-term capital gains chargeable under section 112, where income is computed as per the normal provisions of the Act.

### Suggestion

It is suggested that requisite changes be made in the income-tax utility to provide for rebate u/s 87A in respect of income-tax on long-term capital gains chargeable u/s 112 and short-term capital gains chargeable u/s 111A, where income is computed under the default tax regime u/s 115BAC(1A).

***(SUGGESTION FOR MINIMISING/REDUCING LITIGATION)***

# 7

# DETERMINATION OF TAX IN CERTAIN SPECIAL CASES

## 53. Section 115BBE – Effective rate of 78% on income referred to in sections 68 to 69D - Need to rationalize the rate of tax

### Provision of Law

As per section 115BBE(1), where the total income of an assessee,—

(a) includes any income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D and reflected in the return of income furnished under section 139; or

(b) determined by the Assessing Officer includes any income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D, if such income is not covered under clause (a),

the income-tax payable shall be payable@60% on the income referred to in clauses (a) and (b).

Such income-tax will be increased by surcharge@25% on income-tax and cess@4% on income-tax and surcharge. The effective income-tax rate is, therefore, 78%.

As per section 271AAC, the Assessing Officer or the Joint Commissioner (Appeals) or the Commissioner (Appeals)] may, notwithstanding anything contained in this Act other than the provisions of section 271AAB, direct that, in a case where the income determined includes any income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D for any previous year, the assessee shall pay by way of penalty, in addition to tax payable under section 115BBE, a sum computed at the rate of ten per cent of the tax payable under section 115BBE:

### Issue

Post demonetisation on 8th November, 2016, vide the Taxation Laws (Second Amendment) Act, 2016, which came into force on 15th December, 2016, section 115BBE was substituted w.e.f. A.Y. 2017-18, increasing the amount of tax on income referred to in section 68/69/69A/69B/69D to 60% *plus* surcharge@25% on such tax and cess@4% on tax and surcharge. The effective rate of tax is 78%.

Further, penalty@10% on such tax computed is leviable u/s 271AAC, if the income is not included by the assessee in the return. This provision which was introduced 7 years back post demonetisation, needs to be relooked, considering that section 68 to 69D can be invoked if the explanation given by the assessee is not satisfactory in the opinion of Assessing Officer. The Assessing Officer can therefore invoke the provisions of these sections by exercising his discretionary power.

**Suggestion**

It is suggested that the rate of tax u/s 115BBE be rationalized. It may be kept @ 30% plus surcharge at the applicable rate and cess @ 4%. Penalty@10% of tax payable under section 115BBE may continue.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 54. Section 115BBG - Income from transfer of carbon credits to be taxed @ 10% - Inclusion in definition of income under section 2(24)

**Provision of Law**

Section 115BBG, inserted by the Finance Act, 2017 w.e.f. A.Y.2018-19, provided for tax@10% on income from transfer of carbon credits.

**Issue**

This provision helped resolve the uncertainty and litigation over the taxability of income from the transfer of carbon credits.

Consequent amendment is required in the definition of the term 'income' under Section 2(24) to include the income from transfer of carbon credits.

**Suggestion**

It is suggested that section 2(24) may be amended to include income from transfer of carbon credits in the definition of "income".

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 55. Section 115BBF – Patent Box Regime – Suggestions for rationalisation

### Provision of Law

India introduced its patent box regime vide Finance Act, 2016 with effect from 1st April 2017. Under the regime, royalty income in respect of a patent developed and registered in India shall be taxable at a flat rate of 10%.

### Issue

There are certain concerns in the existing patent box regime which need to be addressed:

(i) The requirement that the patent has to be 'registered' in India - It is unclear as to whether a patent which has been applied for, but for which registration has not been granted will qualify under this regime.

(ii) Coverage of regime has been restricted to Patents - Patent Box regime is not available to other IPRs, like industrial design, copyrights, trademarks, etc.

(iii) No guidelines on outsourcing of IP development - There are no guidelines on outsourcing of R&D functions. Thus, limited outsourcing may also raise an issue on availability of benefit under patent box regime.

(iv) Initial patent developed by individual - The benefit is available to the true and first inventor of the invention. Thus, where a company acquires a patent developed by an individual and invests to develop it further to make it marketable, it may not be eligible for the benefit.

### Suggestion

In order to rationalize the existing Patent Box Regime, it is suggested that:

(i) the benefit of the regime may be obtained where a patent is applied for, but registration has not yet been granted under the Patent law.

(ii) the benefit of the regime may be extended to other forms of IPRs, like industrial design, copyrights, trademarks, etc. so as to promote IPR registration in India.

(iii) the benefit of the regime may be available, subject to a reasonable threshold, in cases where IP development is outsourced.

(iv) the existing regime may be liberalised to grant benefit to a person who acquires patent from the 'true and first inventor' and further makes is commercially usable.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 56. Deduction to entities undertaking Green Projects, Exemption of interest income of subscribers of green bonds issued by such entities and other incentives for promoting climate change mitigation efforts

### Issue

In alignment with global sustainability goals and the Indian government's commitment to combating climate change, tax incentives may be provided for promoting climate change mitigation efforts/strategies.

For example, enhanced tax benefits may be provided for the purchase and use of Electric Vehicles (EVs). This can include additional deduction for businesses investing in EV fleets.

In order to promote efforts to reduce carbon emissions, taxpayers may be incentivized to earn more carbon credits by offsetting their carbon footprints.

Incentives may be given in the form of additional depreciation in the initial year of purchase and installation of solar panels etc. or by way of investment allowance.

Green bonds are a type of debt issued by institutions to finance themselves for green projects that impact the environment positively. They commit the use of the funds obtained through such issue to an environmental project or one related to climate change. In order to encourage green projects, special concessions need to be given to entities issuing such bonds as well as the persons subscribing to such bonds. However, at present, there are no specific exemptions in respect of the same.

### Suggestion

Tax benefits may be provided for promoting climate change mitigation strategies, which will not only contribute to India's climate change goals but also drive economic growth by promoting sustainable business practices.

Incentives may be given in the form of additional depreciation in the initial year of purchase and installation of solar panels etc. or by way of investment allowance.

In order to incorporate the sustainability aspect in taxation, special exemption/deduction may be given to entities undertaking green projects. In the alternative, a concessional rate of tax@15%, akin to the rate of tax in erstwhile section 115BAB may be given to such companies.

The capital gains and interest income earned by the subscribers of green bonds may be exempt or, in the alternative, subject to a concessional rate of tax.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 57. Section 10(23FB) - Tax exemption for Income of a Venture Capital Company/Venture Capital Fund from investment in a Venture Capital Undertaking – Scope of exemption to be expanded

### Provision of Law

Section 10(23FB) exempts any income of a venture capital company or venture capital fund from investment in a venture capital undertaking.

### Issue

Upto 31.3.2008, any income of a Venture Capital Company (VCC) or Venture Capital Fund (VCF) set up to raise funds for investment in a Venture Capital Undertaking (VCU) was exempt under section 10(23FB). However, w.e.f. 1.4.2008, this was amended and the scope of VCC / VCF was narrowed down to select sectors and the exemption from income tax was limited to "any income of a VC company or VC fund from investment in a venture capital undertaking".

Keeping in mind the growing importance of VC funds in infrastructure and also in other important sectors of our economy, the previous wording of "set up to raise funds for investment" may be restored in place of "from investment" under Section 10(23FB).

A change in the wording from "any income of a VC company or VC fund from investment" to "any income of a VC company or VC fund set up to raise funds for investment" will enable the VCC / VCF to undertake analysis / study necessary to evaluate the project viability as well as to render other services for the projects in which investments are made. Restricting the wording to "any income of a VC company or VC fund from investment in a VCU" restricts the tax exemption which may affect the commercial viability of the VCC / VCF.

### Suggestion

It is suggested that section 10(23FB) be reworded as follows:

***"Any income of a venture capital company or venture capital fund set up to raise funds for investment in a venture capital undertaking."***

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

# 8

# TAXATION OF TRUSTS AND INSTITUTIONS

## 58. Section 11 – Taxation of Charitable Trusts and Institutions – Removal of restriction on carry forward of excess application of income and removal of restriction on time for repayment of loan and deposit back in corpus for availing benefit of application

### Provisions of Law

(i) Section 11 has been amended by the Finance Act, 2021 so as to*, inter alia*, deny the benefit of carry forward of excess application of the trust assessee for set off against income of subsequent years.

(ii) As per clause (i) of *Explanation 4* to section 11(1), application for charitable or religious purposes from the corpus shall not be treated as application of income for charitable or religious purposes. However, the amount not so treated as application shall be treated as application in the previous year in which the amount, or part thereof, is invested or deposited back into one or more forms or modes specified in section 11(5) maintained specifically for such corpus, from the income of the year and to the extent of such investment or deposit, provided that such investment or deposit has to be made within 5 years from the end of the previous year in which such application was made from the corpus.

(iii) As per clause (ii) of *Explanation 4* to section 11(1), application for charitable or religious purposes, from any loan or borrowing, shall not be treated as application of income for charitable or religious purposes. However, the amount repaid will be treated as application in the year of repayment and to the extent of repayment, provided that the repayment is made within a period of 5 years from the end of the previous year in which such application was made from loan or borrowing.

### Issues

#### 1. Denial of benefit of carry forward of excess application

The Finance Act 2021 has amended section 11 so as to*, inter alia*, deny the benefit of carry forward of excess application of the trust assessee for set off

against income of subsequent years. Charitable trusts are making a significant contribution in helping build a better world. Their contribution assumes further significance in upliftment of poor, medical relief etc. during the tough times of Covid pandemic, Earthquake, Floods, etc.

However, the restrictions vide the Finance Act 2021 may act as a deterrent to such trusts. Excess application may be required in circumstances such as Covid19 pandemic when Charitable Trusts join hands with the Government and contribute substantially to relief activities. To deny carry forward of such excess application may deter the Charitable Trusts to go the extra mile in supporting the Government in the hour of need. Accordingly, the said provisions need reconsideration.

**2. Restriction that repayment loan taken for charitable purposes has to be made within 5 years and that the amount withdrawn from corpus should be invested or deposited back into the corpus within 5 years for being treated as application**

In case of loan taken for purchase of, say, immovable property for the purposes of the trust, the repayment period may extend to 15 years or more. Restricting the benefit of application to 5 years would cause genuine difficulty to the trust, since the amount repaid from the 6th year would not be treated as application. Similar concern exists with the requirement of depositing back into corpus within 5 years for being treated as application, the amount invested or deposited back out of voluntary contributions from the 6th year would not be treated as application.

**Suggestion**

It is suggested that:

suitable legislative amendments be carried out in section 11 so that the benefit of carry forward may be allowed to the trust in aforesaid cases.

(ii) The restriction relating to investment/deposit back into corpus within 5 years and repayment of loan taken for charitable purposes within 5 years for being treated as application may be removed.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 59. Section 12AB(3) – Time limit for passing an order reckoned from the end of the month in which application is received – Clarification relating to status of registration application in case no order is passed within the time limit specified in section 12AB(3)

### Provision of Law

Section 12AB(3) prescribes the time limit for passing order granting or refusing application for registration of trust or institution made under section 12A(1)(ac). The time limit is 3 months/6 months/1 month, respectively, from the end of the month in which application was received in different cases.

### Issue

If the order granting or refusing application for registration of trust or institution u/s. 12A is not passed within the time limit specified in section 12AB(3) (3 months/6 months/1 month, as the case may be, from the end of the month in which application is received), the status of registration cannot be defined. Some judgments pronounced in relation to section 12AA that it will be considered as deemed registration if no order is passed within the 6 month period stipulated in section 12AA(2), while some judgments are against this view. In order to minimize litigation, it is necessary to clarify that the same will be considered as deemed registration, if no order is passed within the time specified in section 12AB(3).

### Suggestion

It is suggested that, in order to minimise litigation, it may be clarified that non-disposal of application for registration u/s 12A within the time limit specified in section 12AB(3) would be considered as deemed registration.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 60. Section 12A(1)(ac)(iii) – Time limit for making an application for registration of trust or institution, which is provisionally registered – Clarity on the meaning of "Date of Commencement of Activity"

### Provision of Law

Section 12A(1)(ac)(iii) mandates trusts and institutions which have been provisionally registered under section 12AB to make an application for registration to the Principal Commissioner or Commissioner at least six months prior to the expiry of provisional registration or within six months from the "date of commencement of its activities," whichever is earlier.

### Issue

The meaning of "date of commencement of activity" has not been defined/spelt out in the provisions which has led to varying interpretations by the trusts/institutions and Assessing Officers. Consequently, this has resulted in multiple instances of provisional registration applications being denied, even when trusts are acting in good faith to comply with the intended requirements. This ambiguity leads to unnecessary procedural hurdles and avoidable litigation.

Also, due to the different interpretations on the date of commencement of activity, it may be possible for trusts to miss the deadline of "six months from the date of commencement of activity". Since the application has to be filed before the earlier of six months from the date of commencement of activity or at least six months prior to expiry of period of provisional approval, there is a concern of trusts missing the earlier deadline of "six months from the date of commencement of activity"

### Suggestion

It is suggested that an explanation be inserted in clause (iii) of Section 12A(1)(ac), defining the "date of commencement of activity" to mean the date when the trust first started applying its income towards its stated objects.

Also, a proviso may be inserted in sub-clause (iii) of section 12A(1)(ac), which would read as follows –

"*Provided that where the trust or institution has not filed an application within six months of commencement of activities it may do so at any time before the six months prior to expiry of period of the provisional registration or provisional approval, as the case may be*".

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 61. Section 12A(1)(b) read with Rule 17AA – Requirement to maintain books of account and other documents by trusts and institutions for 10 years from the end of the relevant assessment year – Period may be reduced to 6 years from the end of the relevant assessment year

### Provision of law

Section 12A(1)(b) provides that where the total income of a trust or institution computed without giving effect to the provisions of sections 11 and 12 exceed the basic exemption limit, the exemption provisions under sections 11 and 12 would apply only if the books of account and other documents have been kept and maintained in the form and manner prescribed in Rule 17AA.

Rule 17AA(1) prescribes the books of account to be maintained by trusts and institutions. Rule 17AA(4) requires trusts and institutions to keep and maintain their books of account and other documents for a period of 10 years from the end of the relevant assessment year.

### Issue

The requirement of maintenance of books of account and other documents by trusts and institutions for 10 years is much longer and needs to be aligned with the requirements in the other provisions of the Act.

In this context, it may be noted that section 44AA(1) requires persons carrying on specified profession to maintain the books of account and documents prescribed in Rule 6F(2). Rule 6F(5) requires that such books of account be maintained for a period of 6 years from the end of the relevant assessment year.

### Suggestion

It is suggested that Rule 17AA(4) be amended to require trusts and institutions to keep and maintain their books of account and other documents for a period of 6 years from the end of the relevant assessment year.

***(SUGGESTION FOR REDUCING COMPLIANCE BURDEN)***

## 62. Section 13(9) – Time limit for filing return of income by a trust which accumulates income u/s 11(2) – Filing of return to be permitted within the time allowed u/s 139(4)

### Provision of Law

Section 12A(1)(ba) provides that the exemption provisions under sections 11 and 12 will not apply in relation to income of the trust unless the trust has furnished the return of income in accordance with the provisions of section 139(4A) within the time allowed u/s 139(1) or 139(4).

Section 13(9) provides that the benefit of accumulation under section 11(2) will not apply if the return has not been furnished on or before the due date u/s 139(1).

### Issue

As per section 12A(1)(ba), the exemption to the trust will not be denied even if the trust files a belated return u/s 139(4) (i.e., on or before 31st December of the Assessment Year). There has been no corresponding amendment in section 13(9) to permit filing of return of income u/s 139(4) in case of accumulation u/s 11(2). This seems to imply that if the trust wishes to accumulate any part of its income, then, it cannot file a belated return u/s 139(4).

In this context, it may be noted that there is no corresponding provision in section 10(23C), which implies that in case of accumulation by a trust claiming exemption u/s 10(23C), filing of return of income u/s 139(4) would be permissible. Since section 13(9) denies the benefit of extended time limit u/s 139(4) for a trust claiming exemption under sections 11 and 12, the same may be amended to permit filing of return u/s 139(4) for accumulation u/s 11(2). This will ensure alignment of the provisions of the second regime with the first regime.

### Suggestion

Section 13(9) may be amended to permit a trust which accumulates income u/s 11(2) to file its return of income u/s 139(4).

***(SUGGESTION FOR REDUCING/MINIMIZING LITIGATION)***

## 63. Section 115TD(5) – Person liable to pay tax on accreted income to the credit of the Central Government within 14 days from the specified date – Recovery from Principal Officer/trustee to be done only if not-payment is attributable to their gross neglect, misfeasance, breach of duty & Increase in time limit for remittance

### (a) Reconsideration of applicability of recovery provisions and levy of interest for non-payment of tax by specified person on the Principal Officer/trustee

**Provision of law**

**The opening sentence of Section 115TD(5) reads as follows:**

**"The Principal Officer or the trustee of the specified person**, as the case may be, and the specified person shall also be liable to pay the tax on accreted income to the credit of the Central Government within fourteen days from the specified date, in different cases mentioned in clauses (i) to (v) thereunder.

**Issue**

The Assessing Officer can consider almost any person connected with the management as the Principal Officer of the institution. It seems that the primary liability to pay tax is on Principal Officer or the trustee of the specified person as well as the specified person. Consequently, interest under section 115TE for non-payment of tax would be leviable on the Principal Officer and trustee in addition to the specified person. Also, the Principal Officer and trustee would be treated as an assessee-in-default for non-payment of tax on accreted income in accordance with he provisions of section 115TD.

**Suggestion**

It is suggested that -

(i) The recovery provisions (including levy of interest under section 115TE and treating them as an assessee-in-default for non-payment of tax on accreted income) should be made applicable to the Principal Officer/trustee, only if it is proved that non-payment is attributable to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the charitable institution or trust.

(ii) Clarification may be given regarding who can be covered as Principal Officer of the trust.

### (b) Increase in time for remittance of tax on accreted income

**Provision of Law**

As per section 115TD(5), tax on accreted income has to be paid within a period of 14 days.

**Issue**

The time limit of 14 days is too short especially when institution is required to dispose of its assets to make payment. Further, when capital assets are sold, proceeds would also be subject to capital gains tax. If the tax is not paid within 14 days, then interest@1% per month or part of month is attracted under section 115TE. Also, the Principal Officer or the trustee and the specified person is deemed as an assessee-in-default.

**Suggestion**

It is suggested that the time of 14 days may be suitably increased.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 64. Section 10(21) – Exemption of income of a research association – To include within its scope associations engaged in Skill Development Program

**Provision of Law**

Section 10(21) provides for exemption of income of a research association which has as its object undertaking of scientific research or research in social science or statistical research approved for the purpose of section 35(1)(ii)/(iii), subject to fulfillment of specified conditions.

**Issue**

It does not however, include associations/institutions engaged in skill development program or undertaking any other research.

**Suggestion**

It is suggested to include institutions exclusively engaged in Skill Development programs and institutions engaged in other research activities within the scope of exemption under section 10(21).

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 65. Section 115UA(2) – Tax on total income of a business trust at MMR, subject to the provisions of section 111A and section 112 – Reference to section 112A also to be included along with section 111A and 112.

**Provision of law**

As per section 115UA(2), the total income of a business trust shall be charged to tax at the maximum marginal rate, subject to the provisions of Section 111A and Section 112.

This implies that capital gains on transfer of short-term capital assets which are chargeable to tax under section 111A and capital gains on transfer of long-term capital assets chargeable to tax under section 112, will be chargeable to tax at the rates of 20% and 12.5%, respectively.

**Issue**

On the same lines, capital gains on transfer of long-term capital assets referred to in section 112A also has to be charged to tax at the rate of 12.5% and not at MMR. However, there is no reference to section 112A in section 115UA(2).

It is essential to that the chargeability to tax at MMR under section 115UA(2) is subject to the provisions of section 112A along with sections 111A and 112, as the reason for non-inclusion for section 112A is apparently because the section was introduced after section 115UA(2).

**Suggestion**

It is suggested that section 115UA(2) be reworded as follows –

*"Subject to the provisions of section 111A, section 112 and section 112A, the total income of a business trust shall be charged to tax at the maximum marginal rate"*

***(SUGGESTION FOR RATIONALISATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 66. Section 2(29C) - Maximum Marginal Rate – Clarification relating to applicable rate of surcharge for calculation of Maximum Marginal Rate

### Provision of Law

As per section 2(29C), "maximum marginal rate" means the rate of income-tax (including surcharge on income-tax, if any) applicable in relation to the highest slab of income in the case of an individual, association of persons or, as the case may be, body of individuals as specified in the Finance Act of the relevant year

### Issue

In the provisions of the Act where income is subject to tax at MMR (except in cases where surcharge is leviable at a fixed rate of say 12%, like in case of accreted income taxable at MMR u/s 115TD), it is not clear whether MMR has to be calculated applying the highest rate of surcharge or applicable rate of surcharge. As per section 167B, income of an AOP would be chargeable to tax at MMR. If the member is a foreign company chargeable to tax at a rate higher than MMR, the share pertaining to the foreign company would be chargeable at the higher rate. As per section 2(29C), MMR means the rate of income-tax (including surcharge on income-tax, if any) applicable in relation to the highest slab of income as specified in the Finance Act of that year. However, in section 2(9) of the Finance Act, 2023 pertaining to payment of advance tax, in clause (c) of the third proviso thereof pertaining to AOPs consisting of only companies as its members, the surcharge rate of 10% has been specified, where total income > Rs.50 lakhs but < Rs.1 crore; and 15% where total income exceeds Rs.1 crore. Generally, MMR implies application of the highest rate of surcharge, which as per the Finance Act, 2023 has to be restricted to 15% in case of AOPs where all members are companies. However, the stipulation of different surcharge rates in clause (c) of the third proviso to section 2(9) indicates surcharge has to be applied according to the respective slab of total income for computation of MMR. It may be clarified whether applicable slab rate of surcharge or the highest rate of surcharge has to be considered for computing MMR under different provisions of the Income-tax Act, 1961. For example, in case of a business trust, section 115UA(2) provides that the total income of a business trust shall be charged to tax at MMR. In such cases, clarification is required as to whether highest rate of surcharge or applicable slab rate should be considered while computing MMR.

### Suggestion

It is suggested that a suitable clarification be issued at the earliest w.r.t. applicability of rate of surcharge when income-tax has to be computed at maximum marginal rate under the provisions of the Act.

Also, in the case of AOPs with all members being companies, the rate of surcharge must be in alignment with the surcharge rates for companies.

***(SUGGESTION FOR REDUCING/MINIMISING LITIGATION)***

# 9

# PROVISIONS FOR FILING RETURN OF INCOME & ASSESSMENT PROCEDURE

## 67. Section 139(4) & (5) - Time Limit for Filing a Belated Return and Revised Return - Extension of time limit upto 31st March of the relevant assessment year

**Provisions of law**

As per Section 139(4), if any person who has not furnished a return within the time allowed to him under sub-section (1), may furnish the return for any previous year at any time before three months prior to the end of the relevant assessment year or before the completion of the assessment, whichever is earlier.

As per section 139(5), if any person, having furnished a return under sub-section (1) or sub-section (4), discovers any omission or incorrect statement therein, they may file a revised return at any time before three months prior to the end of the relevant assessment year or before the completion of the assessment, whichever is earlier.

**Issue**

As a result, the current deadline to file a belated return and revised return is 31st December of the relevant assessment year.

The additional time to file belated return and revised return is too short. Earlier, it was upto 31 March of the assessment year relevant to previous year. Many taxpayers may only become aware of errors or omissions in their return during the course of assessment proceedings. By this time, the window for filing a revised return has already closed.

**Suggestion**

It is suggested that the due date for filing a belated and revised return under section 139(4) and section 139(5), respectively, be extended to **31st March of the relevant assessment year** instead of 31st December. This will provide taxpayers with more time to reconcile information and correct any omissions or errors.

***(SUGGESTION FOR REDUCING COMPLIANCE BURDEN)***

## 68. Section(s) 139(8A) & 140B - Provisions for filing of updated return – Certain concerns to be addressed

### (a) Enabling provision for reporting reduction in losses in their Updated return

**Provision of Law**

The first proviso to section 139(8A) provides that the provisions of section 139(8A) enabling filing of updated return will not apply if the updated return is a return of a loss or has the effect of decreasing the total tax liability determined on the basis of return furnished under section 139(1)/(4)/(5) or results in refund or increases the refund due on the basis of return furnished under section 139(1)/(4)/(5), of such person under the Act for the relevant assessment year.

**Issue**

The first proviso to section 139(8A) inadvertently misses a situation wherein a person would like to report reduction in losses. Reduction in losses is akin to increase in income and accordingly, should come under the purview of the said provisions. Accordingly, the relevant provisions need to be amended to provide for such a situation wherein an assessee voluntary wishes to file the updated return and report reduction in losses.

**Suggestion**

It is suggested that provisions of section 139(8A) be suitably amended so as to provide for a situation wherein assessees desiring to file updated returns to report reduction in losses be permitted to do so.

(b) **Need to relax certain eligible conditions/exclusions for filing updated returns like assessment proceedings**

**Provision of Law**

Clause (b) of the third proviso to section 139(8A) provides that no updated return shall be furnished by any person for the relevant assessment year, where any proceeding for assessment or reassessment or recomputation or revision of income under the Act is pending or has been completed for the relevant assessment year in his case.

**Issue**

Here, there is a case of relaxing this condition i.e. updated return may be permitted in cases where assessment proceedings have been completed and where assessment proceedings are pending, updated return may continue to be non-permitted. In cases where assessment proceedings are completed, it is clear that concerned taxpayer is coming forward on a voluntary basis as such incomes have not been caught in the assessment proceedings completed. This is also one of the objectives behind introduction of provisions of updated returns.

**Suggestion**

It is suggested that the condition in section 139(8A) pertaining to making assessees ineligible to file updated return in cases where any proceeding for assessment or reassessment or re-computation or revision of income under the Act is pending or has been completed for the relevant assessment year in his case may be suitably relaxed and accordingly allow filing of updated returns wherein assessment proceedings have been completed.

***(SUGGESTION FOR MITIGATING LITIGATION AND IMPROVING TAX COLLECTION)***

## 69. Section 139(9) – Intimation for Defective return – Default Time limit for response to be extended from 15 to 30 days, intimation to be appealable, opportunity of being heard to be provided before treating the return as invalid

### Provision of Law

Section 139(9) reads as follows -

*"(9) 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 from the date of such intimation or within such further period which, on an application made in this behalf, the Assessing Officer may, in his discretion, allow; and if the defect is not rectified within the said period of fifteen days or, as the case may be, the further period so allowed, then, notwithstanding anything contained in any other provision of this Act, the return shall be treated as an invalid return and the provisions of this Act shall apply as if the assessee had failed to furnish the return:*

*Provided that where the assessee rectifies the defect after the expiry of the said period of fifteen days or the further period allowed, but before the assessment is made, the Assessing Officer may condone the delay and treat the return as a valid return."*

### Issue

Under section 139(9), after receiving intimation from the Assessing Officer, the assessee has to rectify the defect within 15 days. The extension of the above period is discretionary. The intimation is, however, not appealable to the Joint Commissioner (Appeals) or Commissioner (Appeals).

With increasing digital processing, even cases where the taxpayer has already declared income, the return may still be flagged as defective.

For example, some deductee-taxpayers are facing an issue where higher income from an earlier previous year is reflected in their Form 26AS in the current financial year. This is on account of tax of an earlier previous year being deducted in the current financial year by the deductor at the time of payment, whereas, the income was reflected in the return of an earlier year by the deductee taxpayer on an accrual basis. The prior year's income on which tax is deducted at source (TDS) in the current year is being matched with the income of the current year. In cases where the prior year's income (as shown in Form No. 26AS of the current year) is higher and the current year's income reflected in the return of income is lower, the consequent mismatch results in the return of income of the current year of the deductee-taxpayer being wrongly treated as defective and issuance of intimation under section 139(9) to him to rectify the defect.

Another example is where assessees who have tax deducted under section 194N

and are duly reported by the tax deductor in the TDS Return are also receiving intimation u/s 139(9) due to a mismatch of income offered for taxation with the amount reported by the tax deductor on which tax has been deducted u/s 194N. Although tax is deducted on cash withdrawals exceeding the specified amount as per section 194N, the same in most cases would not be the income of the taxpayer.

Also, in some cases, intimation for defective return is issued for classification of income under a different head.

Intimation in such cases creates undue hardship for the assessee, who may have correctly reported income but still gets an intimation to rectify the defect.

Explanation to section 139(9) enlists the conditions to be fulfilled for a return of income to be regarded as defective. This Explanation needs a relook in the e-filing regime to specify in a clear manner as to the cases where the return of income can be treated as defective. This will help ensure that returns are flagged only when there is a genuine issue with the return filed.

Further, the default period to rectify the defect is only 15 days, which is a very short period to prepare and submit a well-supported response. If the tax payer does not rectify within this period, the return would be treated as an invalid return. There is no provision requiring providing an opportunity of being heard to the assessee.

**Suggestion**

It is suggested that *Explanation* to section 139(9) be amended to specify in a clear manner the conditions to be fulfilled for treating a return of income defective in the e-filing regime.

Further, intimation under section 139(9) should be treated as an order appealable before the Joint Commissioner (Appeals)/CIT(A).

Also, it is suggested to extend the default response period for addressing defective notice from the current 15 days to 30 days. Also, a return of income should be treated as invalid, only after providing the assessee an opportunity of being heard. This is in line with the principles of natural justice.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 70. Section 143(1)(a) – Prima facie adjustments to the total income – To be restricted to adjustments to verify arithmetical accuracy

### Provisions of law

**Section 143(1)(a) reads as follows -**

143 (1) Where a return has been made under section 139, or in response to a notice under sub-section (1) of section 142, such return shall be processed in the following manner, namely:—

(a) the total income or loss shall be computed after making the following adjustments, namely:—

(i) any arithmetical error in the return;

(ii) an incorrect claim, if such incorrect claim is apparent from any information in the return;

(iii) disallowance of loss claimed, if return of the previous year for which set off of loss is claimed was furnished beyond the due date specified under sub-section (1) of section 139;

(iv) disallowance of expenditure or increase in income indicated in the audit report but not taken into account in computing the total income in the return;

(v) disallowance of deduction claimed under section 10AA or under any of the provisions of Chapter VI-A under the heading "C.—Deductions in respect of certain incomes", if the return is furnished beyond the due date specified under sub-section (1) of section 139; or

(vi) addition of income appearing in Form 26AS or Form 16A or Form 16 which has not been included in computing the total income in the return:

However, no adjustment shall be made under sub-clause (vi) in relation to a return furnished from A.Y.2018-19.

### Issue

Section 143(1)(a) provides the adjustments which can be made while processing the return of income of an assessee.

The adjustments listed out in sub-clauses (i) to (v) of section 143(1)(a) are prima facie adjustments which are to be made in the course of computerized processing without any human interface. In other words, the software is designed to detect arithmetical inaccuracies and incorrect claims apparent from any information in the return and make appropriate adjustments in the computation of the total income.

However, in many cases, the adjustments made u/s 143(1)(a) go beyond the sub-clauses (i) to (v) listed therein.

For example, in many cases, claim of foreign tax credit (FTC) for taxes paid in a country with which India has a DTAA is denied while processing return under section 143(1)(a), even if the assessee has duly uploaded Form No.67 verified by him. This defeats the purpose of allowing double taxation relief u/s 90.

Another example is when stamp duty valuation on the date of registration which formed the basis of TDS u/s 194-IA by the buyer is being considered for adjustment u/s 143(1)(a) in the hands of the seller in respect of capital gains computation, even through section 50C permits adoption of stamp duty value on the date of agreement, if atleast some portion of the consideration was paid otherwise than by way of cash on or before the date of agreement. Such adjustments need to be avoided u/s 143(1)(a).

The automatic disallowance of genuine claims during the initial processing stage, often without proper verification, leads to unintended consequences, including increased litigation and taxpayer grievances.

Also, there are cases where the response filed by the assessee in relation to the adjustment is not considered nor any response is provided for not accepting the assessee's stand.

Consequently, in such cases, the assessee has to make an application u/s 154 for rectification or file an appeal before Joint Commissioner (Appeals)/Commissioner (Appeals), thereby adding to the pendency of appeals before these authorities.

**Suggestion**

Section 143(1)(a) be specifically limited to addressing only arithmetical errors and prima facie incorrect claims. By restricting the scope of adjustments to clear mathematical inconsistencies and manifest errors, the possibility of disallowing legitimate exemptions and deductions can be significantly reduced.

Intimation under section 143(1)(a) to be issued after providing for an opportunity of being heard to the assessee.

Existing disputes relating to section 143(1)(a) be permitted to be settled through arbitration.

## 71. Section 158B(b) – Definition of Undisclosed Income – To exclude "any expense, deduction or allowance claimed under the Act which is found to be incorrect" therefrom, since the same is not consequent to search or requisition

### Provision of Law

The Finance (No.2) Act, 2024 has reintroduced the block assessment in case of search initiated or requisition made on or after 1st September 2024, by substitution of new Chapter for Chapter XIV-B with effect from 1st September, 2024.

As per clause (b) of section 158B, "Undisclosed income" includes any money, bullion, jewellery or other valuable article or thing or any expenditure or any income based on any entry in the books of account or other documents or transactions, where such money, bullion, jewellery, valuable article, thing, entry in the books of account or other document or transaction represents wholly or partly income or property which has not been or would not have been disclosed for the purposes of this Act, or any expense, deduction or allowance claimed under this Act which is found to be incorrect, in respect of the block period.

Tax would be levied@60% on such undisclosed income.

### Issue

The definition of "undisclosed income" should include such components which can be backed by incriminating material found in the course of search. However, the scope of definition in section 158B(b) is too wide and includes expenses, deduction or allowance claimed under the Act which is now found to be incorrect. These expenses, deduction etc. would have been allowed in the assessment u/s 143(3). They are not unearthed as a result of search or requisition. Bringing such expenses now within the scope of "undisclosed income" under block assessment would give rise to a spate of litigation.

### Suggestion

It is suggested that the last portion of clause (b) of section 158B, namely, "or any expense, deduction or allowance claimed under this Act which is found to be incorrect" be removed from the definition of "undisclosed income", since the same is not consequent to search or requisition and can give rise to avoidable litigation.

***(SUGGESTION FOR REDUCING/MINIMIZING LITIGATION)***

# 10

# DEDUCTION, COLLECTION AND RECOVERY OF TAX

## 72. Chapter XVII-B – Provisions relating to deduction of tax at source - TDS rates may be pegged at maximum of 2%, aligning with the objective of serving as an audit trail

**Provision of Law**

The Finance (No.2) Act, 2024 has reduced the rates of TDS under section 194-DA, 194G, 194H, 194-IB and 194M to 2% w.e.f. 1st October, 2024 to improve ease of doing business and better compliance by tax payers.

**Issue**

Certain other TDS provisions however still require tax deduction at a higher rate like section 194, 194A, 194-IC, 194-LA, 194R etc. These rates also need to be rationalized.

**Suggestion**

In line with the intent of TDS provisions serving as an audit trail rather than a revenue garnering measure, TDS rates under all provisions where the rate is higher than 2%, may be pegged at maximum of 2%. This will increase the working capital available and minimize the possibility of disputes arising from the incorrect application of rates.

This will increase the working capital available and minimize the possibility of disputes arising from the incorrect application of rates as well as improve compliance and minimize litigation.

***(SUGGESTION FOR REDUCING/MINIMISING LITIGATION)***

## 73. Section 206C(1G) – TCS on the remittance of funds outside India – need to rationalize the rates of TCS

### Provision of Law

The rates of TCS under section 206C(1G) on the remittance of funds outside India are 5% and 20%, depending on the amount and purpose of remittance. The concessional rate of 0.5% is only where an amount in excess of Rs.7 lakh being remitted out is a loan from a financial institution for educational purpose. If the source is own funds remitted out for educational purpose, the rate would be 5% for amount in excess of Rs.7 lakh. For other than medical and educational purposes, the rate is 20% for remittance in excess of Rs.7 lakh. For overseas tour package, the rate of TCS is 5% upto Rs.7 lakh and 20% thereafter.

### Issue

The rates of TCS are high, particularly considering that such transactions are purely for tracking purposes.

### Suggestion

It is suggested that the TCS rates of 5% and 20% under section 206C(1G) be rationalized and reduced to 2%.

This will increase the working capital available and minimize the possibility of disputes arising from the incorrect application of rates as well as improve compliance and minimize litigation.

**(Suggestion for mitigating litigation and providing tax certainty)**

## 74. Section 194A- TDS on interest on compensation amount awarded by the Motor Accidents Claims Tribunal – Case for exemption of such interest from income-tax and TDS

### Issue

There are court rulings holding that Motor Accident Claim Tribunal (MACT) is a capital receipt and hence, do not fall within the definition of "income" under Income-tax law and hence, is not taxable. Other reasons are, MACT compensation is a compensation for agony, loss of mobility, physical damage and loss of earnings suffered by the victim, granted by courts and not compensation granted under statutory provision.

MACT compensation is a subject matter of litigation. The following sections in Income-tax Act, 1961 deal with the same -

(1) Section 194A(3)(ixa) requiring tax to be deducted on interest on compensation awarded by MACT, where the aggregate amount of income paid during the financial year exceeds Rs 50,000.

(2) Section 145A(b) requires that interest received on compensation or enhanced compensation shall be accounted on receipt basis,

(3) Section 56(2)(viii) providing for taxability of income received on compensation or on enhanced compensation referred to in Section 145A(b) under the head "Income from other sources" and section 57(iv) allowing deduction of 50% of income referred to section 56(2)(viii).

Even though section 145A(b), 56(2)(viii) and 57(iv) speak about compensation generally, section 194A(3)(ixa) specifically requires TDS on Interest on Motor Accident Claim Tribunal. Although the provisions for TDS and computation of total income are separate under the system of income-tax, the requirement to deduct tax on interest on MACT leads to an understanding that the interest is taxable under the Act.

1. There are various legal decisions which has ruled that MACT compensation is *ab-initio* not an income. Actually, when something is not at all an income and does not fall under the purview of Income-tax Act, 1961 for taxation, there is no need to give an exemption under section 10. Only those income which are otherwise taxable, and as a relief measure, Government wants to exempt it, exemption under 10 is to be provided. Even disaster compensation mentioned under section 10(10BC) is not an income *ab-initio* for giving an exemption. However, insertion of such exemption is clarificatory in nature and puts an end to any possible litigation. Hence for MACT compensation also, on similar lines, an exemption provision may be incorporated in the Act.

2. Persons who are getting claim under MACT are those who have already

undergone suffering in their life and sometimes they are getting compensation fighting at court and after waiting for years. Hence, this clarification is required in the Act so that they need not be subject to tax after getting compensation. As a social measure, suitable amendment and clarity may be brought under the Income-tax law.

**Suggestion**

It is suggested to -

(1) remove TDS on interest awarded by Motor accident claim Tribunal and

(2) insert a specific exemption under section 10 for amount received on Compensation, enhanced compensation and interest on compensation awarded by Motor Accident Claim Tribunal.

194A(3)(ixa) may be omitted and in section 194A(3)(ix), word 'or paid' can be inserted between 'credited' and 'by way of interest'. Accordingly, section 194A(3)(ix) may be worded as under –

*"(ix) to such income credited or paid by way of interest on compensation amount awarded by the Motor Accidents Claims Tribunal"*

There are separate exemptions available under 10(10B) for compensation received by a workman under Industrial Dispute Act, under section 10(10BB) for any payments received under the Bhopal Gas Leak Disaster (Processing of Claims) Act and section 10(10BC) for compensation received from Government on account of any disaster. Likewise, it is may be worded as follows -

*"any amount received or receivable by way of compensation or enhanced compensation or otherwise (including interest thereon) awarded by the Motor Accident Claim Tribunal".*

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 75. Section 194A - Interest other than interest on securities – Exemption from TDS on interest credited or paid to an NBFC & Introduction of TCS provision

### Provision of Law

Section 194A(3)(iii)(a) provides that the tax on interest other than interest on securities is NOT required to be deducted by a person responsible for paying the same to a resident, if the income is credited or paid to any banking company to which Banking Regulation Act, 1949 applies or any co-operative society engaged in the business of banking (including a co-operative land mortgage bank).

### Issue

It may be noted that Section 194A does not treat Non-Banking Financial Institutions (NBFCs) at par with the Banking companies or Co-operative Banks. Due to this, the middle-class businessmen who have borrowed money from NBFC's are disallowed interest paid on the same while computing their business income, due to non-deduction of tax at source under section 194A. It is suggested that exemption from applicability of TDS under section 194A be provided in respect of income credited or paid to an NBFC due to the following reasons:

a) There is no mechanism for deduction of tax on interest paid by the assessees as the NBFCs collect cheques of EMI for the tenure of loan.

b) NBFCs principal business is of lending money under various products just like a banking company or a co-operative bank.

c) NBFCs are also regulated by RBI just like Banking Company and a Co-operative Bank.

Considering the fact that there is no mechanism for deduction of tax on interest paid by the assessees as the NBFCs collect cheques of EMI for the tenure of loan, the non-compliance of the provisions of this section is inevitable. However, the requirement to deduct tax is a cause of concern for the assessee who has borrowed money as he is unable to claim deduction in respect of said interest due to operation of section 40(a)(ia).

### Suggestion

To provide relief to the genuine taxpayers paying interest to NBFC's, it is suggested that section 194A(3)(iii)(a) be amended to treat NBFCs at par with other banking companies. Further, in order to ensure compliance of the provisions of the Act for timely collection of taxes, provisions of tax collection at source be made applicable to NBFCs in respect of such interest.

***(SUGGESTION FOR IMPROVING TAX COLLECTION)***

## 76. Section 194J - Fees for professional or technical services – Increase in independent threshold limits for attracting TDS & provision of independent threshold for TDS on director's remuneration

### Provision of Law

Section 194J requires deduction of tax at source@10% on any remuneration or fees or commission, by whatever name called, to a director of a company, other than those on which tax is deductible under section 192.

### Issue

The independent limit of Rs.30,000 each provided for under section 194J in respect of other payments covered therein, namely, royalty, fee for technical services, fee for professional services and non-compete fees, as a threshold, beyond which TDS would be attracted, is, however, not being provided in respect of director's remuneration. This unintended inequity may be removed.

Also, the limit of Rs.30,000 was fixed 14 years back in 2010. The limit may be suitably increased considering the inflation factor.

### Suggestion

It is suggested that -

1. the independent threshold of Rs 30,000 may be increased to Rs.1,00,000 considering the inflation factor.
2. an independent threshold be provided in respect of remuneration or fees or commission to director above which the sum may be subject to tax deduction at source.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 77. Section 194N - TDS on cash withdrawals from one or more accounts maintained with a bank, co-operative society carrying on banking business and post office – TDS to be restricted to cash withdrawals from current account

### Provision of Law

Section 194N requires every person being a bank, a co-operative society carrying on the business of banking and a post office, who is responsible for paying any sum being the amount or aggregate of amounts, as the case may be, in cash exceeding Rs.1 crore during the previous year, to any person from one or more accounts maintained by the recipient with it to deduct 2% of such sum as income-tax.

### Issue

Para 126 of the budget speech (Union Budget 2019) reads as follows - (relevant extract reproduced below):

"To promote digital payments further, I propose to take a slew of measures. To discourage the practice of making business payments in cash, I propose to levy TDS of 2% on cash withdrawal exceeding Rs. 1 crore in a year from a bank account." [emphasis supplied]

The Hon'ble Finance Minister referred to discouraging 'business' payments in cash while introducing provisions of section 194N. Payments for business are usually made from 'current account' maintained with banks. However, the text of section 194N, as inserted by the Finance (No. 2) Act, 2019, levies TDS on withdrawal from all types of accounts, be it current or saving or any other account maintained by the recipient.

### Suggestion

It is suggested that the intent expressed in the budget speech for introducing section 194N, i.e., discouraging making of business payments in cash, may be suitably incorporated in the text of section 194N i.e. withdrawals from only current account may be taken into account for TDS purposes.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 78. Section 194T – Tax@10% to be deducted by the firm responsible for paying any sum in the nature of salary, remuneration, commission, bonus or interest to a partner of the firm – Reconsideration of the provision or reduction of rate to 2%

### Provision of Law

The Finance (No.) Act, 2024 has inserted section 194T to require deduction of tax at source@10% by a firm, responsible for paying any sum in the nature of salary, remuneration, commission, bonus or interest to a partner of the firm, at the time of credit of such amount to the account of the partner (including the capital account) or at the time of payment thereof, whichever is earlier.

Where such sum or, the aggregate of such sums credited or paid or likely to be credited or paid to the partner of the firm does not exceed Rs.20,000 during the financial year, no tax will be deducted at source. This amendment will take effect from 1st April, 2025, i.e., A.Y.2025-26 (P.Y.2024-25).

The Explanatory Memorandum does not contain the rationale for introduction of such provision except stating that presently there is no provision for deduction of tax at source on payment of salary, remuneration, interest, bonus or commission to partners by the partnership firm.

### Issue

Pursuant to the amendment, tax is required to be deducted by the firm at the time of credit of sum as referred above to any category of account (including the capital account) or at the time of payment, whichever is earlier.

The intention of the partners and partnership firm doing business together is to derive profits to be distributed between them. If the business requires the funds back, the partners may not even withdraw the funds or they would reinvest the funds back to business of the firm. Partners final sharing is possible to be determined only on final net results derived on the year end; till that time, it is generally an internal understanding of the funds withdrawal. In effect, to what extent the funds withdrawal during the year includes salary or remuneration can be determined only at the end of the year, when the net result is derived.

Consequent to insertion of section 194T, it becomes necessary to carefully estimate the income of the partners as well as income of the firm at the beginning of the financial year based on which remuneration / bonus is to be forecasted and may need to be incorporated in the partnership deed. There may be instances where income of the partner (other than income of from the firm) may be increased/ decreased by substantial amount resulting in increase/ decrease in the effective tax rate of partner than effective tax rate of the firm. In such a case, if the amount withdrawn is tagged as remuneration and subjected to TDS, it may become burdensome. Further, there may be instances where if tax under section 194-T has already been deducted, and thereafter, the firm decides not to pay the remuneration since the profitability as expected could not be achieved or the firm's profits have

substantially decreased due to unforeseeable circumstances, then, the firm has no option but to revise the remuneration and as also the TDS returns of the earlier months.

In any case, since advance tax is payable by the firm and partners, and short payment of advance tax would attract interest u/s 234C, there is no need for a separate TDS provision.

Further, where as per the agreement of partnership, a fixed sum is payable as remuneration every month, only the remuneration upto the limits permitted u/s 40(b) would be deductible in the hands of the firm and chargeable to tax in the hands of the partner. The allowable remuneration is based on "book profit" which can be determined only after the end of the year. The balance remuneration would be disallowed in the hands of the firm. Hence, it would not be chargeable in the hands of the partners. However, TDS@10% is deductible on the entire remuneration and not only the amount which is actually subject to tax in the hands of the partners.

Alternatively, in order to ease the burden of tax, it may be considered to reduce the proposed rate from 10% to 2%. TDS@10% is very high and would significantly impact the cash flow of partners, particularly in small and medium-sized firms. Reducing the rate to 2% would alleviate this burden, enabling partners to reinvest funds into the business and facilitate growth. It may be mentioned that the rates of TDS under sections 194DA, 194G, 194H, 194-IB and 194-M have ben reduced to 2% with effect from 1st October, 2024, to improve ease of doing business and better compliance by taxpayers. Bringing Section 194T also in line with these sections by reducing the rate of TDS to 2% will help address the issue of cash flow concerns.

**Suggestion**

It is suggested that the amendment as proposed in section 194T be reconsidered and withdrawn. Instead, the amount paid to partners can be captured in the Annual Information Statement, which would help track payments by the firm to partners.

Alternatively, the rate of TDS under section 194T may be reduced from 10% to 2%, in line with the reduction in the rates of TDS by the Finance (No.2) Act, 2024 in other sections.

***(SUGGESTION FOR REDUCING COMPLIANCE BURDEN)***

## 79. Section 194R - Guidelines for deduction of tax on benefit or perquisite in respect of business or profession - Relief from penal consequences arising due to scope for different interpretation - Need for clarity in guidelines

### Provision of Law

As per section 194R, any person responsible for providing to a resident, any benefit or perquisite, arising from business or the profession, shall, before providing such benefit or perquisite, ensure that tax has been deducted in respect of such benefit or perquisite at the rate of ten per cent of the value or aggregate of value of such benefit or perquisite.

Further, no tax is required to be deducted, if the value or aggregate of value of the benefit or perquisite provided or likely to be provided to such resident during the financial year does not exceed twenty thousand rupees.

### Issue

Despite the two clarificatory circulars issued immediately after the introduction of section 194R, i.e., Circular No. 12/2022 and Circular No. 18/2022 for providing guidelines for removal of difficulties under sub-section (2) of section 194R, this provision remains challenging for taxpayers to comply with, leading to potential inadvertent non-compliance. The ambiguity in its interpretation, combined with the inherent complexity, poses difficulty for taxpayers and results in unintended penal consequences. This provision, if not simplified, may lead to increased litigation and hardship for businesses.

### Suggestion

It is suggested to simplify the guidelines so that they are clear, unambiguous and leave no scope for different interpretation; so as to facilitate ease of compliance. Additionally, we suggest introducing a mechanism for taxpayers to rectify genuine mistakes caused on account of different possible interpretations without attracting penal consequences including prosecution.

***(SUGGESTION FOR MINIMISING/REDUCING LITIGATION)***

## 80. Section 197A – Furnishing of declaration in prescribed form for non-deduction of tax at source under specified sections – Inclusion of section 194C in the list of sections

### Provision of Law

In case the recipient of any sum or income or amount, on which tax is deductible at source, fails to furnish PAN to the deductor, section 206AA requires deduction of tax at a higher rate of 20% or the rate or rates in force or the rates specified in the relevant provision of the Act.

Section 197A(1A) provides for furnishing of declaration in prescribed form in writing by a person (not being company or firm) to the effect that tax on his estimated total income of the previous year is Nil. The declaration has to be furnished to the person responsible for paying income referred to in section 192A, 193, 194A, 194D, 194DA, 194-I and 194K.

### Issue

Section 194C is not included in the list of sections in section 197(1A) in respect of which such declaration can be furnished.

### Suggestion

It is suggested that provisions of section 197A(1A) may be extended to the persons covered under section 194C who have income below taxable limit and can give a proper declaration.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 81. Rule 37BB – Information in Part A of Form 15CA to be filled if amount of payment or aggregate of payments made during the financial year does not exceed Rs.5 lakh – Threshold limit to be increased to Rs.10 lakh

### Provision of law

As per Rule 37BB of the Act, remitters are required to file Form 15CA to provide information about remittances made to non-residents, In Part A of Form No. 15CA, if the amount of payment or the aggregate of such payments, as the case may be, made during the financial year does not exceed five lakh rupees. If the payments exceed this amount, then, certificate from Assessing Officer u/s 197 or an order from Assessing Officer under section 195(2)/(3) in respect of information in Part B of Form 15CA. Also, certificate from an Accountant would be required for information in Part C of Form 15CA.

### Issue

The threshold limit has been Rs.5 lakh since 1.4.2016. Considering that almost 9 years have elapsed since then and given the increase in international transactions as well as the general increase in remittance volumes over recent years, it is suggested that the threshold limit upto which information in Part A of Form No.15CA will suffice be increased from Rs.5 lakh to atleast Rs.10 lakh.

### Suggestion

It is suggested that the limit prescribed in Rule 37BB(1)(i) of the Income-tax Rules, 1962 be increased from Rs. 5 lakh to at least Rs.10 lakh.

***(SUGGESTION FOR REDUCING COMPLIANCE BURDEN)***

## 82. Section 200 read with Rule 31A/ Section 285BA(2) read with Rule 114E(5) – Due date for furnishing statement of TDS for quarter ended 31st March and due date for furnishing statement of financial transaction for the financial year – Need for advancing the due date from 31st May to 15th May

**Issue**

The due date for filing the income-tax return for non-corporates and non-audit assessees is 31st July of the assessment year. Taxpayers rely on the updated information in Form 26AS for filing the return. This is available only after mid June, since the due date for filing the statement of TDS for the quarter ended 31st March is 31st May as per Rule 31A. Therefore, taxpayers are left with a short window to verify and reconcile their TDS details before filing their income tax return.

Also, the statement of financial transaction required to be furnished under sub-section section 285BA(1) of the Act shall be furnished in respect of a financial year in Form No. 61A on or before the 31st May, immediately following the financial year in which the transaction is registered or recorded as per Rule 114E(5).

The information available in this statement is also relied upon by taxpayers for filing return.

**Suggestion**

It is suggested that the due date for filing the Q4 TDS return be advanced from 31st May to 15th May. This adjustment will ensure that Form 26AS is updated earlier, allowing non-corporate, non-audit taxpayers sufficient time to reconcile their TDS details and file their returns within the statutory due date of 31st July.

Also, the due date for furnishing the Statement of Financial Transactions (SFT) return also be advanced to 15th May to ensure that information on financial transactions is reflected in Form 26AS in a timely manner, thus aiding taxpayers in accurately reporting such details in their returns.

***(SUGGESTION FOR REDUCING/MINIMIZING LITIGATION)***

## 83. Section 201 – Order deeming a person as an assessee in default - Time limit for passing an order under section 201 be aligned with the time limit for completion of assessment

### Issue

An assessment is carried out by the Assessing Officer under section 143(3) or section 147, as the case may be, whereas order deeming a person as an assessee in default is passed by jurisdictional TDS officer under section 201.

Non-deduction of TDS leads to initiation of TDS proceedings under section 201. It is often seen that while the TDS proceedings are still ongoing, the information is also shared with the Assessing Officer to carry out the assessment / reassessment to make the disallowance of expenses under section 40(a)(i) or 40(a)(ia) for non-deduction of tax at source. This is done inspite of the TDS proceedings being in progress and not concluded.

While the assessment needs to be concluded within a year, TDS proceedings often continue thereafter. This leads to the situation where addition is made under section 40(a)(i) or 40(a)(ia) during assessment while TDS proceedings may be eventually dropped or may still continue, opening avenues for litigation by the assessees.

### Suggestion

To address this concern, the timeline for completing the TDS proceedings be further curtailed and aligned with the timelines for assessment.

***(SUGGESTION FOR REDUCING/MINIMIZING LITIGATION)***

## 84. Section 201(1A) – Interest payable for failure to deduct tax or remit tax after deduction – Manner of computing interest

**Provision of Law**

Section 201(1A) provides for levy of interest for failure to deduct tax or after deduction, to remit the tax deducted within the time prescribed. As per section 201(1A), such person shall be liable to pay simple interest, —

(i) at one per cent for every month or part of a month on the amount of such tax from the date on which such tax was deductible to the date on which such tax is deducted; and

(ii) at one and one-half per cent for every month or part of a month on the amount of such tax from the date on which such tax was deducted to the date on which such tax is actually paid,

and such interest shall be paid before furnishing the statement in accordance with the provisions of sub-section (3) of section 200

**Issue**

Interest is payable@1% per month or part of the month from the date on which tax is deductible till the date on which the tax is deducted; and @1.5% per month or part of the month from the date on which such tax is deducted to the date on which such tax is actually paid.

Accordingly, if tax deductible on 22nd January, 2025 has been deducted on 15th March, 2025 and the tax so deducted has been paid on 10th June, 2025, then interest u/s 201(1A) has to computed as follows –

@1% per month for 2 months (22/1/2025-21/2/2025 and 22/2/2025-15/3/2025)

@1.5% per month for 3 months (15/3/2025-14/4/2025, 15/4/2025-14/5/2025 and 15/5/2025 -10/6/2025)

However, the TRACES portal calculates the interest considering the calendar months, as given below –

@1% per month for 3 months (January, Feb and March, 2025)

@1.5% per month for 4 months (March, April, May and June, 2025)

The calculation based on calendar month is not equitable and correct. Even a one day delay in remittance can result in levy of interest@1.5% p.m. for 2 months. For example, tax deducted in the month of February has to be deposited on or before 7th March. If it is deposited on 8th March, interest@1.5% p.m. will be levied for 2 months (Feb and March).

**Suggestion**

It is suggested that changes be made in the TRACES portal so that for the purpose of calculating interest under section 201(1A), a month should not be reckoned as a calendar month.

Instead, interest under clause (i) of section 201(1A) has to be calculated reckoning a month as beginning from the date on which tax was deductible to the date immediately preceding the said date in the next month. For example, if the date on which tax is deductible is 22nd January, then, 22nd Jan to 21st Feb may be reckoned as the first month; 22nd Feb to 21st March as the second month, and so on. If the tax deduction is made on 15th March, then, interest has to be calculated under clause (i) of section 201(1A)@1% p.m. for 2 months.

Likewise, interest under clause (ii) of section 201(1A) has to be calculated reckoning a month as beginning from the date on which tax was deducted to the date immediately preceding the said date in the next month. Continuing the above example, if the date on which deduction is made is 15th March, then, 15th March to 14th April is to be reckoned as the first month; 15th April to 14th May is to be reckoned as the second month; and 15th May to 14th June is to be reckoned as the third month, and so on. If the payment is made on 10th June, interest has to be calculated under clause (ii) of section 201(1A)@1.5% p.m. for 3 months.

***(SUGGESTION FOR REDUCING/MINIMIZING LITIGATION)***

## 85. Section 230(1A) - Obtaining Income Tax Clearance Certificate by persons domiciled in India who have outstanding direct tax arrears exceeding Rs.10 lakhs – Threshold to be increased to Rs.50 lakhs

### Provision of law

Section 230(1A) relates to obtaining of a tax clearance certificate, in certain circumstances, by persons domiciled in India. The said provision, as it stands, came on the statute through the Finance Act, 2003 w.e.f. 1.6.2003.

CBDT clarification in respect of Income-tax clearance certificate (ITCC) via press release dated 20th August 2024 contains reference to Instruction No. 1/2004, dated 05.02.2004, as per which the tax clearance certificate under Section 230(1A) of the Act may be required to be obtained by persons domiciled in India only in the following circumstances -

(i) where the person is involved in serious financial irregularities and his presence is necessary in investigation of cases under the Income-tax Act or the Wealth-tax Act and it is likely that a tax demand will be raised against him, or

(ii) where the person has direct tax arrears exceeding Rs. 10 lakh outstanding against him which have not been stayed by any authority.

### Issue

Considering the inflation rates and the volume of business transactions over the past two decades, the threshold of Rs.10 lakh is low and needs to be increased substantially.

### Suggestion

It is suggested for obtaining the Tax Clearance Certificate, the threshold of outstanding direct tax arrears which have not been stayed by any authority be increased from Rs. 10 lakh to Rs. 50 lakh, taking into account factors such as inflation, the ease of doing business, the growth of the economy, and the increased volume of high-value transactions.

***(SUGGESTION FOR REDUCING COMPLIANCE BURDEN)***

## 86. Section 234C – Interest on deferment of advance tax – Benefit of non-levy of interest in earlier installment(s) where capital gains has arisen thereafter be extended even while calculating interest under section 234C, where book profit is deemed as total income under section 115JB

### Provision of Law

234C levies interest on shortfall in payment of advance tax instalments. In respect of income from capital gain, where failure to estimate such income might arise, the current law allows to deposit the advance tax on such income without interest in remaining instalments.

### Issue

Where assessee is subjected to MAT for any previous year and profit on sale of capital asset included in profit and loss account is also subjected to MAT, then, section 234C does not provide specific exclusion from levy of interest on account of failure to estimate such income. Even if such income has accrued to the assessee in the month of March and assessee is subjected to MAT provisions, demand is determined and interest on shortfall is calculated on advance tax payment from 1st instalment itself.

### Suggestion

It is suggested that profit on sale of capital asset recognised in books shall be treated in parity with income from capital gain and accordingly, interest u/s 234C may not be levied, even in a case where book profit is deemed as the total income under section 115JB.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 87. Section 234B/234C -Interest for delay in payment of advance tax and interest for deferment of advance tax - Rationalisation of rate of interest on advance tax computed on estimated income.

**Provision of Law**

Interest is levied u/s 220(2) @1% every month or part of month, if the amount specified in the notice of demand under section 156 is not paid within 30 days of the service of notice.

Interest is levied at the same rate of 1% per month or part of month u/s 234C for deferment of advance tax on the amount of shortfall.

**Issue**

In case of levy of interest u/s 220(2), there is a default in payment of tax and hence, the levy is justified. However, interest is levied at the same rate of 1% per month or part of month u/s 234C for deferment of advance tax on the amount of shortfall. Since advance tax is computed on estimated income and not actual income, it is not justified that the assessee be subject to the same rate of interest for failure to estimate his income correctly as he is subject to for failure to pay tax on actual income for which notice of demand is issued. In this context, it may be noted that interest on refund is calculated @½% for every month or part of month u/s 244A.

**Suggestion**

It is suggested that the rate of interest u/s 234B and 243C may be rationalized considering that advance tax is paid on estimated income and not on actual income and that the rate of interest on refunds is calculated at only ½% per month or part of month u/s 244A.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 88. Section 244A- Interest on Refunds – Time limit to be specified for credit of refund to the assessee's account after issuance of order/intimation granting refund

### Provision of Law

As per section 244A, where refund of any amount becomes due to the assessee under the Income-tax Act, 1961, he shall be entitled to receive, in addition to the said amount, simple interest thereon@0.5% for every month or part of a month upto the date on which the refund is granted.

### Issue

In practice, there is often a significant delay between the order or intimation granting the refund and the actual receipt of the refund, largely due to accounting or administrative delays at the Centralized Processing Centre (CPC). However, no interest is payable for the period between the issuance of the refund order and the actual receipt of the refund by the assessee.

### Suggestion

It is suggested that a specific time limit be prescribed, within which the refund should be credited to the assessee's account after the issuance of an order granting the refund to ensure that refunds are processed in a timely manner.

Also, in case of delay beyond the prescribed time limit, additional interest should be granted to the assessee. This will ensure accountability and encourage timely processing.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 89. Section 197 – Certificate of no deduction of tax at source – Inclusion of section 194-IA within its scope

### Provision of Law

Section 197 provides for issuance of certificate for non-deduction of tax at source or deduction at lower rates under certain sections by the Assessing Officer, if he is satisfied that total income of the recipient justifies deduction of income-tax at lower rates or no deduction of tax, as the case may be.

### Issue

The provisions for tax deduction under section 194-IA on consideration for transfer of immovable property is causing hardship to those sellers who claim full capital gains exemption by investing the capital gains or the net consideration, as the case may be, in the manner provided in section 54, 54F, 54EC etc., since in such cases, there would be no tax liability on account of capital gains. Further, for the purposes of section 54F, the entire net consideration is required to be invested, which would pose a difficulty, since tax would already have been deducted from the net consideration.

### Suggestion

It is, therefore, suggested that section 197 may be amended to permit the assessee intending to claim exemption under sections 54/54F/54EC to make an application to the Assessing Officer for issuing a certificate for no deduction of tax or deduction of tax under section 194-IA at a lower rate.

***(SUGGESTION FOR RATIONALISATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 90. Section 197A(1F) – No deduction of tax to be made in case of payments to notified persons or class or persons – Extension of benefit to commission retained by bank while making payments to Merchant Aggregators and commission retained by Merchant Aggregators while making payments to Merchants

### Provision of Law

As per section 197A(1F), no deduction of tax is to be made or tax is to be deducted at lower rates from such payment to such notified person or class of persons, including institution, association or body or class of institutions, associations or bodies, as may be notified, by the Central Government in this behalf.

### Issue

As part of promoting cashless transactions and converting India into less-cash society, various modes of digital payments are available. These modes are regular banking channels which is Credit Card and Debit Card, where generally, Bank is the merchant acquirer.

In the light of government's push on digital payments, the concept of Merchant Aggregator/Acquirer has come up where the Merchant Aggregator is not the bank, but a separate entity. Merchant Aggregator acquires various merchants and ties up with banks for processing of payments. The Merchant Aggregator collects money from banks on behalf of its merchants and then makes the final settlement with its merchants. The Merchant Aggregators are an integral part of the overall Digital Payment system which act as a conduit between customers, bank and merchant. These Merchant Aggregators collect money from customer's bank/PPI Wallet and make payment to merchants.

In a move aimed at encouraging the transition towards a cashless economy, the CBDT has exempted some payments made to banks and payment service providers from deducting tax at source. These payments include credit card or debit card commissions for transactions between a merchant establishment and the bank.

CBDT vide its Notification No. SO 3069(E), dated 31-12-2012, has notified that no deduction of tax under Chapter XVII shall be required on payments of the nature given below, in case such payment is made by a person to a bank, namely:-

*(vii) Credit card or debit card commission for transaction between merchant establishment and acquirer bank*.

Exemption under section 197A(1F), as given above, was introduced considering the problems being faced by merchants, where merchants received the transaction value net of bank commission from bank and there was no instance where the merchant made any payment to the bank and hence, it was not feasible for any merchant to

withhold tax under the TDS provisions from Bank. Due to the above technical reason, merchants were exempted from the provisions of TDS when the commission was payable to Banks. With new technology and newer ways of making and accepting payments, it is imminent to widen the scope of this exemption.

When Merchant Aggregator receives payment from bank for ultimate settlement with merchant, bank makes the payment to Merchant Aggregator after deducting its commission. The Merchant Aggregator, at no instance, gets any chance to withhold tax since it is only receiving payments and not making any payment to Bank.

In the above instances, while the scenario is similar to the exemption given under powers as per section 197A(1F) and appearing in clause (vii) of the exemption list, still the exemption is limited to cases where the commission is received by bank from the merchant establishment.

**Suggestion**

It is suggested that -

(i) MDR retained by bank from Merchant Aggregator and by Merchant Aggregator from Merchant Establishment may be exempted from TDS.

(ii) The exemption u/s 197A(1F) may be extended to cases:

- where the commission is retained by the bank while making payment to Merchant Aggregator (as the Income-tax department may consider Merchant Aggregator on a different footing with Merchant Establishment); and
- where the commission is retained by the Merchant Aggregator while making payment to Merchants

The above suggestion will remove the deterrent for merchant aggregators as they will be in line with merchant establishment. This move will encourage online transactions by reducing the compliance burden as the merchant establishment will not have to deduct TDS before making the payment to the Merchant Aggregators.

This will also make the whole process seamless and the merchants will not be wary to accept the new modes of payment due to the additional compliance of withholding tax. This will encourage the merchants to move from cash to digital

***(SUGGESTION FOR REDUCING/MINIMISING LITIGATION)***

## 91. Section 206AA– Higher rate of TDS where PAN is not linked with Aadhar – Notice for demand to be quashed if PAN is linked with Aadhar on or before the due date of filing of return

### Provisions of Law

As per section 206AA, any person entitled to receive any sum or income or amount, on which tax is deductible under Chapter XVIIB (hereafter referred to as deductee) shall furnish his Permanent Account Number to the person responsible for deducting such tax (hereafter referred to as deductor), failing which tax shall be deducted at the higher of the following rates, namely:—

(i) at the rate specified in the relevant provision of this Act or

(ii) at the rate or rates in force or

(iii) at the rate of twenty per cent

### Issue

PAN becomes inoperative if the same is not linked with Aadhaar on or before 31st December, 2024, except in the case of exempted category of persons. One of the consequences is that where tax is deductible under Chapter XVII-B in case of such person, such tax shall be deducted at a higher rate in accordance with the provisions of section 206AA; and in case where tax is collectible at source under Chapter XVII-BB in case of such person, such tax shall be collected at higher rate, in accordance with the provisions of section 206CC.

Several deductors and collectors of tax, who have deducted and collected tax at the normal rate instead of the higher rate under section 206AA applicable to assessees whose PAN had become inoperative due to non-linkage with Aadhar, have received income tax demand notices intimating that they have committed default of "short deduction/collection" of tax and asking them to deposit the short deduction in TDS/TCS. These deductors and collectors were not aware that the deductee's/collectee's PAN had become inoperative.

### Suggestion

It is suggested that if PAN is linked with Aadhaar on or before the due date of filing of return of income, then, the demand notices sent to deductors/collectors for "short deduction/collection of tax" be quashed.

***(SUGGESTION FOR MINIMISING/REDUCING LITIGATION)***

## 92. Introduction of year-wise E-Ledger system for crediting TDS/TCS and advance tax payments which can be adjusted against the income-tax due

**Issue**

There are several instances of mismatches in case of TDS claimed and TDS allowed while processing return u/s 143(1)(a). In some cases, such mismatches also lead to issuance of intimation u/s 139. For example, some deductee-taxpayers are facing an issue where higher income from an earlier previous year is reflected in their Form 26AS in the current financial year. This is on account of tax of an earlier previous year being deducted in the current financial year by the deductor at the time of payment, whereas, the income was reflected in the return of an earlier year by the deductee taxpayer on an accrual basis. The prior year's income on which tax is deducted at source (TDS) in the current year is being matched with the income of the current year. In cases where the prior year's income (as shown in Form No. 26AS of the current year) is higher and the current year's income reflected in the return of income is lower, the consequent mismatch results in the return of income of the current year of the deductee-taxpayer being wrongly treated as defective and issuance of intimation under section 139(9) to him to rectify the defect. This is one such example. There are several other instances of mismatch.

**Suggestion**

It is suggested that an **year-wise E-ledger mechanism**, similar to the one implemented in respect of the Goods and Services Tax (GST), be introduced for income-tax payments also. The key benefits of the e-Ledger system in GST include providing a transparent, real-time overview of tax credits, cash balances, and set off of liabilities. A similar system can be effectively implemented for income tax to improve ease of doing business, enhance compliance, and increase operational efficiency.

The **year-wise income-tax e-Ledger** would capture all advance tax payments made, the TDS/TCS credits which can be adjusted against the tax due for the current previous year. The balance credit, after adjusting the tax due, may be refunded to the assessee or allowed to be carried forward to the next year for adjustment against tax due in that year. On the other hand, if the tax due is more than the credit, the assessee can pay the same by way of self-assessment tax.

***(SUGGESTION FOR MINIMISING/REMOVING COMPLIANCE BURDEN)***

# 11

# APPEALS & REVISION

## 93. Section 254(2) - Time Limit for Amendment of Orders passed by the Appellate Tribunal under Section 254(1) – Need for enhancement of the time limit

**Provision of Law**

**Orders of Appellate Tribunal.**

Section 254(1) and (2) read as follows -

254. (1) The Appellate Tribunal may, after giving both the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit.

(2) The Appellate Tribunal may, at any time within six months from the end of the month in which the order was passed, with a view to rectifying any mistake apparent from the record, amend any order passed by it under sub-section (1), and shall make such amendment if the mistake is brought to its notice by the assessee or the Assessing Officer.

**Issue**

Prior to the amendment made by the Finance Act, 2016 w.e.f. 1.6.2016, the time limit for such amendments was four years from the date of the order. With the transition to Faceless Tribunals, effective from June 2021, the procedure in appeal and passing order has undergone significant changes. While this shift aims to reduce delay and enhance transparency, it may also necessitate a more flexible timeline for rectifying any inadvertent mistakes or addressing additional grounds that may be raised.

**Suggestion**

It is suggested that the time limit for amendment of orders under Section 254(2) be extended from the current six months to one year from the end of the month in which the order was passed.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

# 12

# PENALTIES & PROSECUTIONS

## 94. Section 270A - Levy of penalty in case of under reporting of income and misreporting of income – Certain Issues to be addressed

### a) Non-consideration of TDS and advance tax paid while computing penalty

**Provision of Law**

As per section 270A(3)(i)(a), in a case where income has been assessed for the first time and return has been furnished, the amount of underreported income shall be the difference between the income assessed and the income determined under section 143(1)(a).

As per section 270A(3)(i)(b), in a case where income has been assessed for the first time and no return of income has been furnished, the amount of under-reported income shall be the amount of income assessed, in case of a firm or company. In other cases, it will be the difference between the amount of income assessed and the maximum amount not chargeable to tax.

The time limit for imposition of penalties is contained in section 275. The time limit under residuary clause (c) of section 275(1) is, in any other case, after the expiry of the financial year in which the proceedings, in the course of which action for the imposition of penalty has been initiated, are completed, or six months from the end of the month in which action for imposition of penalty is initiated, whichever period expires later.

**Issue**

There are certain concerns arising out of the provisions of section 270A. There may be initiation of penalty several years after the assessment proceedings are completed.

Clause (c) of *Explanation 4* to section 271(1)(c) provided for deduction of advance tax, TDS and TCS from tax on income assessed to arrive at the amount of tax sought to be evaded. However, in section 270A, where return of income is not furnished, penalty will be calculated with reference to tax on income assessed without considering the impact of tax deducted or advance tax paid by taxpayer. For example, in case of a person who is not required to furnish return of income under section 115A(5), tax may have been paid, but, as per this methodology, the whole of the income, as assessed, may be considered as unreported income.

Such would also be the case in a situation where there is no revenue loss since the whole of the tax was already paid and yet, the return may not have been furnished.

**Suggestion**

Without prejudice thereto, with regard to this methodology of levying penalty, it is suggested that -

(i) By way of express requirement, the Assessing Officer may be required to initiate the proceedings prior to or concurrently with the closure of assessment proceedings.

(ii) In cases where income has been assessed for the first time but no return is filed, section 270A may be amended to provide for calculation of tax payable on under-reported income as increased by the basic exemption limit as if it were the total income, and giving credit for TDS/TCS and advance tax therefrom.

(iii) Penalty proceedings may be permitted only when specific conditions are satisfied. e.g. the adjustment made exceeds a minimum threshold or say 10% of taxable income, etc.

## b) Order to specify the specific clause of under reported or misreported income for levy of penalty under section 270A

**Issue**

Section 270A imposes penalty at the rate of either 50% or 200% depending on whether the income is under reported or misreported. Certain controls may be required for the effective implementation of the section.

In order to ensure that the Assessing Officer does not treat every underreported income as misreported as well as the fact that the section does not require recording of satisfaction before imposition of penalty proceedings (as was required under the erstwhile section 271), it is desirable that a suitable control mechanism be put in place. Certain measures like making it mandatory for the Assessing Officers to mention in the Order that every disallowance or addition be specified as either under-reported or misreported.

Further, measures like specifying the exact clause of section 270A(9), in case of misreporting of income (wherever applicable) in the order would go a long way in reducing disputes and litigation. The said measures would also make it clear to the assessee in time whether he could opt for immunity from penalty and

prosecution under section 270AA in case order specifies that he has not misreported the income.

**Suggestion**

It is suggested that suitable amendments be introduced under section 270A so that each order contains the specific fact of misreported income (wherever applicable) along with the mention of specific clause of section 270A(9) against each disallowance/addition. Such measures would act as a suitable control mechanism in the absence of recording of satisfaction to initiate penalty proceedings and would also enable assessee to opt for section 270AA providing for immunity from penalty and prosecution in case income is not misreported.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 95. Section 270AA - Immunity from Imposition of penalty not available in case of misreporting of income – Remedy where certain additions are on account of under-reporting and certain additions are on account of misreporting.

### Provision of Law

As per section 270AA, an assessee can make an application to the Assessing Officer to grant immunity from imposition of penalty under section 270A. However, the Assessing Officer can grant immunity from imposition of penalty under section 270A, only where the proceedings for penalty have not been initiated on the ground of misreporting.

### Issue

Where penalty is levied on certain additions on ground of mis-reporting and certain additions on ground of only under-reporting then the assessee will have to make a choice whether to file appeal or make application for immunity as he cannot file appeal on penalty levied on mis-reported income and immunity application for under-reported income.

### Suggestion

It is suggested that suitable provision be inserted to address this issue.

***(SUGGESTION FOR RATIONALIZATION OF THE PROVISIONS OF DIRECT TAX LAWS)***

## 96. Section 271AAD – Penalty for false entry, etc., in books of account – Certain concerns to be addressed

### Provision of Law

Section 271AAD(1) provides for a levy of penalty, if it is found during any proceeding under the Act that in the books of account maintained by any person, there is a

(i) false entry; or

(ii) omission of any entry relevant for computation of total income of such person, to evade tax liability.

As per *Explanation* to section 271AAD, for the purposes of this section, "false entry" **includes** use or intention to use -

(a) Forged or falsified documents such as a false invoice or, in general, a false piece of documentary evidence; or

(b) invoice in respect of supply or receipt of goods or services or both issued by the person or any other person without actual supply or receipt of such goods or services or both; or

(c) Invoice in respect of supply or receipt of goods or services or both to or from a person who does not exist.

### (a) Amendment in section 271AAD(i) requiring penalty to be attracted only when false entry is made with an intent to evade tax liability

#### Issue

Clause (i) of section 271AAD(1) mentions only 'false entry' without the specific requirement that such false entry 'which is relevant for computation of total income of such person', must have been made with an intent to evade tax liability for penalty to be attracted.

There is a possibility of a false entry emanating later due to recasting of books and/or errors/omissions. Since the definition of 'false entry' in the *Explanation* to section 271AAD is an inclusive one, there is a possibility that the penalty may be invoked in respect of cases not specifically listed in clauses (a) to (c) thereunder. Therefore, the definition must be an exhaustive one and penalty should be attracted only when such entry has been made with an intent to evade tax liability.

**Suggestion**

It is suggested that:

(i) The section 271AAD(1)(i)/(ii) be suitably amended as below:

*"271AAD. (1) Without prejudice to any other provisions of this Act, if during any proceeding under this Act, it is found that in the books of account maintained by any person there is—*

*(i) a false entry; or*

*(ii) an omission of any entry*

*which is relevant for computation of total income of such person, to evade tax liability* (underlined portion moved from clause (ii) to the long line under clause), *the Assessing Officer may direct that such person shall pay by way of penalty a sum equal to the aggregate amount of such false or omitted entry."*

(ii) The definition of "false entry" in the *Explanation* to section 271AAD(1) should be an exhaustive one and not inclusive, in order to clearly define the scope of the provision and avoid unnecessary litigation.

## (b) Consequential amendment required in section 273B as a 'reasonable cause' for penalty imposed under section 271AAD

**Issue**

Section 273B provides for sections wherein penalty is not imposable if the assessee proves that there was reasonable cause for the said failure. However, section 271AAD is not included in the list of sections therein. Every assessee deserves a reasonable opportunity of being heard especially in case where such high penalty is imposed. The very purpose of enacting section 273B is to allow assessees to explain his case and if reasonable cause for non-compliance is found, such penalty is not to be imposed. Accordingly, section 273B may be amended to include within its scope, penalty to be imposed under section 271AAD also.

**Suggestion**

It is suggested that section 273B be amended so as to include within its scope, penalty imposable under section 271AAD also.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 97. Section 271D & 271E – Penalty for failure to comply with the provisions of section 269SS/269T – Rationalisation of rate of penalty

### Provision of Law

As per section 271D & 271E, if a person accepts/repays a loan or deposit or specified sum/advance, as the case may be in contravention with the provisions of section 269SS/269T, he shall be liable to pay, by way of penalty, a sum equal to the amount of loan or deposit.

### Issue

Penalty of a sum equal to the amount of loan or deposit is on the higher side. The penal provisions of section 271D & 271E may be restricted to 30% instead of 100% of the amount of loan or deposit taken or repaid in violation of provisions u/s 269SS & 269T.

### Suggestion

It is suggested to restrict the levy of penalty to 30% instead of 100% of the amount of loan or deposit taken or repaid in violation of provisions u/s 269SS & 269T.

Also, the provisions of section 269T should not be attracted where debt is converted into equity.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 98. Section 269ST & 271DA – Mode of undertaking transactions & levy of penalty on receipt of any sum in contravention of the provisions of section 269ST - Uniform expression be used in sections 269ST and 271DA

**Provision of Law**

Section 269ST is on the mode of undertaking transactions. The section requires that no person shall receive an **amount** of Rs. 2 lakh or more in aggregate from a person in a day or in respect of a single transaction or in respect of transactions relating to one event or occasion from a person, otherwise than by way of account payee cheque/bank draft/prescribed electronic modes.

Under section 271DA, if a person receives any **sum** in contravention of the provisions of section 269ST, he shall be liable to pay, by way of penalty, a sum equal to the amount of receipt.

**Issue**

The expression, 'amount' has been used u/s 269ST whereas the expression 'sum' has been used u/s 271DA, which may create confusion and result in avoidable litigation.

**Suggestion**

It is suggested that a uniform expression, 'amount' or 'sum of money' may be used at both the places i.e. under section 269ST as well as under section 271DA.

***(SUGGESTION FOR MINIMIZING/REDUCING LITIGATION)***

## 99. Section 271FA – Penalty for failure to furnish statement of financial transaction or reportable account - Clarity regarding the authority to whom an appeal shall lie in case of penalty order passed by DIT

### Provision of Law

Section 271FA provides that if a person who is required to furnish the statement of financial transaction (SFT) or reportable account (RA) under section 285BA(1), fails to furnish such statement within the prescribed time, then the income-tax authority prescribed under section 285BA(1) may direct such person to pay penalty of five hundred rupees for every day of default. Prescribed Income-tax authority as per section 285BA(1) is Director of Income-tax (Intelligence and Criminal Investigation) {DIT} or the Joint Director of Income-tax (Intelligence and Criminal Investigation) as per Rule 114E(4)(a).

Further, section 246A(1)(q) provides that any assessee or any deductor or any collector aggrieved by an order imposing a penalty under Chapter XXI may appeal to the Commissioner (Appeals).

### Issue

Due to certain conflicting judicial decisions, an issue has arisen regarding the authority to whom an appeal shall lie in case of penalty order passed under section 271FA by DIT.

Section 246A(1)(q) provides that any assessee or any deductor or any collector aggrieved by an order imposing a penalty under Chapter XXI may appeal to the Commissioner (Appeals).

However, there are some Tribunal rulings that appeal against an order of Director of Income-tax passed under section 271FA is to be filed before Tribunal who is higher in rank and not before Commissioner (Appeals) who is equivalent in rank with Director of Income-tax.

In order to reduce litigation with regard to this provision, clarification is sought on the aforesaid issue.

### Suggestion

It is suggested that an amendment be made in relevant sections (section 246A or section 253) to clearly specify the authority to whom an appeal may lie against an order passed by DIT under section 271FA.

***(SUGGESTION FOR MINIMISING/REDUCING LITIGATION)***

## 100. Section 276B – Prosecution provisions not to be attracted if tax deducted is deposited at any time before the time prescribed for filing the quarterly statement of TDS – Relief to be extended where tax is deposited before the service of notice

### Provisions of Law

Under clause (a) of section 276B, rigorous imprisonment for a term which shall not be less than three months but which may extend to seven years and with fine are attracted for failure to pay tax after deduction to the credit of the Central Government as required by or under the provisions of Chapter XVII-B.

A proviso has been inserted to section 276B to provide that the prosecution provisions thereunder would not apply if such payment has been made to the credit of the Central Government at any time on or before the time prescribed for filing the statement for such payment under section 200(3).

### Issue

The provisions of section 276B are intended to discourage tax deductors from retaining the legitimate government dues unjustly. However, at ground level implementation, notices are being issued for initiation of prosecution proceedings under section 276B even in cases where tax deductors have deposited the tax deducted by them voluntarily after the stipulated time but before any notice has been served upon them. The initiation of prosecution proceedings in cases of voluntary deposit of TDS after the stipulated time but before service of notice is causing undue hardship to genuine tax deductors. Voluntary remittance of TDS before issue of notice clearly indicates the absence of any mala fide intention on the part of the tax deductors to retain the taxes due to the government. The tax deductors are, in any case, being subject to higher interest@1.5% per month or part of a month under section 201(1A) for the period of delay in remittance. The TDS statements submitted by them also clearly reflect the taxes deducted, the date of deduction and the date of remittance along with interest, which indicates the bona fide intent on the part of the deductors to report the correct details to the Department. However, it appears that the notices for prosecution are issued on the basis of these information provided by the tax deductors in their TDS statements. It is a settled law that prosecution proceedings are appropriate only in cases where deductors deliberately do not deposit the TDS, since mens rea or a guilty mind is a sine qua non for attracting prosecution provisions.

The proviso to section 276B gives relief from prosecution provisions if tax has been paid to the credit of the Central Government at any time on or before the time prescribed for filing quarterly statement under section 200(3).

It is suggested that the relief from prosecution provisions under section 276B be extended to deductors who have paid tax to the credit of the Central Government after the prescribed time limit but voluntarily at time before service of any notice.

**Suggestion**

The proviso to section 276B may be modified to read as under –

*"Provided that the provisions of this section shall not apply if the payment referred to in clause (a) has been made to the credit of the Central Government at any time on or before the service of notice".*

***(SUGGESTION FOR MINIMISING/REDUCING LITIGATION)***

# 13

# MISCELLANEOUS PROVISIONS

## 101. Section 159 – Legal Representatives - Hardship in obtaining 'Legal Heir Certificate' for the purpose of registering deceased assessee's legal heir as representative assessee for e-filing of tax returns of a deceased assessee

### Provision of Law

Section 159(3) provides that *"the legal representative of the deceased shall, for the purposes of this Act, be deemed to be an assessee."*

### Issue

The legal representative of the deceased assessee, thus, needs to comply with various provisions like filing of return, payment of taxes, complying with assessment proceeding on behalf of the deceased assessee.

Filing of tax returns electronically is mandatory for assessees except a few exceptions as provided in Rule 12. The existing procedure to register oneself as legal representative of deceased assessee for filing return of income of deceased assessee is described in brief as below:

a. The legal representative needs to register himself as 'Legal Heir' on the E-Filing portal in order to file return of deceased assessee. This is for the period that Income was earned by the deceased but cannot be returned by him since he has since passed away.

b. Request needs to be made through E-Filing portal for above registration by providing certain details of deceased assessee along with certain specified documents.

c. The following are the documents which are to be submitted/ uploaded: i) Copy of Death Certificate; ii) Copy of PAN of deceased; iii) Self attested PAN copy of the Legal Heir; iv) Legal Heir Certificate issued by the Court/Local Revenue Authority or Surviving member certificate issued by the Local Authority or Pension Order issued by Central/State Government or Registered will.

d. On fulfilling the above details, one can submit the request and will be provided an acknowledgement along with a Transaction ID.

e. The department would then 'accept/reject' the request based on the details and documents uploaded. Where request has been rejected, department will provide the ground for rejection, which can be viewed by clicking on Transaction ID.

All the documents as specified in sub-point 'c' above, are generally available or can be easily obtained except for those specified in (iv). The issues faced for obtaining 'Legal Heir' certificate are as under:

a. Obtaining legal heir certificate or Surviving member certificate from Court/ Local revenue authority is very time consuming as well as a cumbersome.

b. Pension Order is issued by Central/State Government only to its employees and thus any person other than government employee would not be able to obtain the Pension Order.

c. While a will may be available in various cases, registration of a will is not mandatory. Getting a will registered subsequent to the demise of an assessee is not possible.

Thus, taking up a case of a person who is neither a government employee nor in possession of registered will, the only option left for him is to approach Court/Local revenue authority to obtain the said certificate, which is generally a very complex exercise with heavy monetary obligations in terms of cost and time.

The utility permits registration as a legal representative only upto 31st December immediately following the year of death of the person, being the date upto which a belated return u/s 139(4) can be filed. However, it may sometimes take two years to get legal heir certificate from the Court. At that point of time, the utility does not permit registration as a legal representative.

**Suggestion**

Considering the aforesaid concerns, it is suggested that -

**a**. Filing of the documents at (i) to (iii) of (c) should be made as sufficient compliance (i.e. Copy of Death Certificate, Copy of PAN of deceased and Self attested PAN copy of the Legal Heir).

**b.** One of the following alternatives be provided in place of legal heir Certificate:

i) Affidavit from the legal heir or,

ii) Certificate of nomination from institutions like banks or,

iii) Copy of Ration Card specifying the name and relation with the legal heir.

This change may be suggested to be brought about by way of an administrative Circular from the CBDT

**c. The entire process for registering as legal heir should be simplified, and the time restriction for registering as a legal representative should be removed.**

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 102. Section 245 – Set-off and withholding of refunds in certain cases – Opportunity of being heard to be given to the person of the action proposed to be undertaken

### Provision of Law

As per section 245(1), where under any of the provisions of this Act, a refund becomes due or is found to be due to any person, the Assessing Officer or Commissioner or Principal Commissioner or Chief Commissioner or Principal Chief Commissioner, as the case may be, may, in lieu of payment of the refund, set off the amount to be refunded or any part of that amount, against the sum, if any, remaining payable under this Act by the person to whom the refund is due, after giving an intimation in writing to such person of the action proposed to be taken under this sub-section.

Section 245(2) provides that where a part of the refund is set off under the provisions of section 245(1), or where no such amount is set off, and refund becomes due to a person, and the Assessing Officer, having regard to the fact that proceedings for assessment or reassessment are pending in the case of such person, is of the opinion that the grant of refund is likely to adversely affect the revenue, he may, for reasons to be recorded in writing and with the previous approval of the Principal Commissioner or the Commissioner, as the case may be, withhold the refund up to the date on which such assessment or reassessment is made.

### Issue

There are cases where the demand for an earlier year was not accepted by the person who filed for a rectification application under section 154. In a subsequent year, he has a refund. However, instead of getting a refund, he gets an intimation u/s 245 that the same has been adjusted against the demand for the earlier previous year. The person has to submit a response to the intimation under section 245 within 30 days of receiving it. When he does not respond to the intimation within 30 days, outstanding demand will be considered for adjustment against his refund after considering interest on demand. Though the assessee has the option to disagree with the demand, it causes genuine hardship to him. If he misses submitting the response within 30 days, the refund will be adjusted against the outstanding demand. There are cases where the refunds for subsequent years are being adjusted against such non existing demand even after submitting response to intimation under section 245 within 30 days not to adjust against such non-existing demand.

Also, in some cases, where the assessee had preferred Vivad se Viswas Scheme and had paid the entire amount as demanded under VseV and Form 5 being Order for full and final settlement has already been issued by the Principal CIT, yet the non-existing demand has not been removed/deleted/rectified from the Portal. In such cases also,

the refunds for subsequent years are being adjusted against such non existing demand even after submitting response to intimation under section 245 within 30 days not to adjust against such non-existing demand.

**Suggestion**

In order to address the concerns, it is suggested that suitable mechanism be in place to address the concern of refunds being set-off against non-existing demands. Further, the order under section 245 may be made appealable to Appellate Tribunal.

***(SUGGESTION FOR MINIMISING/REDUCING LITIGATION)***

## 103. Rule 3 of Part A of the Fourth Schedule to the Income-tax Act, 1961 – According of recognition to Provident Fund - Codify timeline for approval of application for recognition of Provident Fund within 6 months

### Provision of Law

As per Rule 77, an application for recognition shall be made by the employers maintaining a recognised provident fund for which recognition is sought.

As per Rule 3(1) of Part A of the Fourth Schedule to the Income-tax Act, 1961, the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner may accord recognition to any provident fund which satisfies the conditions prescribed in rule 4. Rule 78 provides that an order according recognition to a provident fund shall take effect from the last day of the month in which the application for recognition is received by the income-tax authority concerned, unless, at the request of the employer, the last day of any later month in the same financial year is specified.

### Issue

As per the Provident Fund Act, 1952, the establishment's employer and employee can create a provident fund scheme by forming a trust, and funds are invested as per rules prescribed under the specified provisions of the Income-tax Act, 1961. The application for approval of recognised provident fund is made to the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner, who may accord recognition to any provident fund which satisfies the conditions prescribed in rule 4. Till now, there is no timeline provided in the Income-tax Act, 1961 within which the approval has to be given by the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner. Sometimes, approval of application for RPF is pending for a long period of time and the assessee is unable to know the status of such application i.e., whether the same has been accepted or rejected.

### Suggestion

It is suggested that Rule 3 of Part A of the Fourth Schedule/Rule 78 be suitably amended to provide for timeline for approval/rejection of application of recognized provident fund be provided. It may also be provided that if no communication is received within the timeline specified, regarding acceptance or rejection of application, the same shall be deemed to be approved.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 104. Provision of social security benefits to tax payers

### Issue

In developed nations, there is a concept of social security to help citizens tide over monetary issues at an advanced age. A similar concept can be implemented in India as well for tax payers. For instance, a very small percentage, say 2% to 5%, of taxes paid by each tax payer can be invested in the form of annuities in his/her name till the tax payer attains the age of 60. Once the tax payer attains the age of sixty, he/she would receive the accumulated amount as a form of social security or pension. This scheme would provide financial support to taxpayers post retirement, create a sense of belonging, and demonstrate the government's recognition of their contribution to nation-building. It would also promote taxpayer compliance.

### Suggestion

It is suggested that a very small percentage, say 2% to 5%, of taxes paid by each tax payer can be invested in the form of annuities in his/her name till the tax payer attains the age of 60. This will encourage the tax compliance and reward honest tax payers.

***(SUGGESTION FOR IMPROVING TAX COLLECTION)***

# 14

# INTERNATIONAL TAXATION

## 105. Explanation *5* to Section 9(1)(i) & Section 47(vicc)- Provisions regarding indirect transfer of capital asset situated in India and exemption of capital gains on transfer of such asset, being shares of an Indian company, on demerger – Both sections to be aligned to include reference to shares of a foreign company deriving its value substantially from assets located in India.

### Provision of Law

*Explanation* 5 to section 9(1)(i) provides that shares of a foreign company which derive, directly or indirectly, its value substantially from the assets located in India shall be deemed to be situated in India.

Section 47(vicc) provides that transfer of shares of a foreign company (which directly or indirectly derives its value substantially from shares of an Indian company) by the demerged foreign company to the resulting foreign company under a scheme of demerger will not be regarded as transfer, subject to satisfaction of the conditions stipulated thereunder.

### Issue

While *Explanation 5* to section 9(1)(i) provides that shares of a foreign company which derive directly or indirectly its value substantially from the assets located in India shall be deemed to be situated in India, section 47(vicc) provides exemption only if the shares of foreign company derive its value substantially from shares of an Indian company. While the intent may be to exempt all cases of demerger where foreign company derives its value substantially from assets located in India, the reading of Section 47(vicc) indicates that the said exemption would be available only in cases where the shares of the foreign company derive its value substantially from shares of Indian company.

Due to this inconsistency in the language of section 47(vicc) *vis-à-vis Explanation 5* to

section 9(1)(i), transfer of shares of a foreign company which derives its value predominantly from assets located in India (other than shares of an Indian company) under a scheme of demerger may be deprived of the aforesaid exemption.

**Suggestion**

It is suggested that –

(i) Section 47(vicc) be amended to provide that "any transfer in a demerger, of a capital asset, being a share of a foreign company, referred to in Explanation 5 to section 9(1)(i), which derives, directly or indirectly, its value substantially from the assets located in India, held by the demerged foreign company to the resulting foreign company, if,— ……..."

(ii) a similar amendment may also be made under section 47(viab) (in case of amalgamation).

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 106. Section 9 - Income deemed to accrue or arise in India on account of Significant Economic Presence – To be limited to digital transactions and obligation to deduct tax only after notification of rules for attribution of income to such transactions or activities

### Provision of Law

Section 9 provides for nexus rule, which if satisfied, deems income to accrue or arise in India and accordingly be taxable in India under the domestic law. The concept of 'Significant Economic Presence' (SEP) has been introduced in the Income-tax Act, 1961, pursuant to which a non-resident having SEP in India would be considered to have a 'Business Connection' (taxable presence) in India. The threshold for SEP has been notified by insertion of Rule 11UD to the Income-tax Rules, 1962.

*Explanation 2A* and *Explanation 3A* to section 9(1)(i) read with Rule 11UD provides that–

Significant economic presence of a non-resident in India shall constitute "Business Connection" in India if -

a) transaction in respect of any goods, services or property carried out by a non-resident with any person in India including provision of download of data or software in India, if the aggregate of payments arising from such transaction or transactions during the previous year exceeds Rs 2 crores; or

b) Systematic and continuous soliciting of business activities or engaging in interaction exceeds 3 lakh users in India.

The above transactions or activities shall constitute SEP, whether or not the agreement for such transactions or activities is entered in India or the non-resident has a residence or place of business in India or the non-resident renders services in India:

Given the above, if the SEP of the non-resident is constituted in India, the income attributable to the transactions or activities as indicated above (i.e. purchase of goods, download of data etc.) would be deemed to be income accruing and arising in India and will be liable to tax in India.

### Issue

### (a) Scope of Significant Economic Presence

The provisions related to "Significant Economic Presence" were first introduced by the Finance Act, 2018. The Explanatory Memorandum to the Finance Bill, 2018 reads as follows -

"*OECD under its BEPS Action Plan 1 addressed the tax challenges in a digital economy wherein it has discussed several options to tackle the direct tax challenges arising in digital businesses. One such option is a new nexus rule based on "significant economic presence". As per the Action Plan 1 Report, a*

*non-resident enterprise would create a taxable presence in a country if it has a significance economic presence in that country on the basis of factors that have a purposeful and sustained interaction with the economy by the aid of technology and other automated tools. It further recommended that revenue factor may be used in combination with the aforesaid factors to determine 'significance economic presence'.*

*The scope of existing provisions of clause (i) of sub-section (1) of section 9 is restrictive as it essentially provides for physical presence-based nexus rule for taxation of business income of the non-resident in India. Explanation 2 to the said section which defines 'business connection' is also narrow in its scope since it limits the taxability of certain activities or transactions of non-resident to those carried out through a dependent agent. Therefore, emerging business models such as digitized businesses, which do not require physical presence of itself or any agent in India, is not covered within the scope of clause (i) of sub-section (1) of section 9 of the Act.*

*In view of the above, it is proposed to amend clause (i) of sub-section (1) of section 9 of the Act to provide that 'significant economic presence' in India shall also constitute 'business connection'".*

From a reading of the above paragraphs it is clear that the intent of introducing "significant economic presence" in section 9 is to bring into its fold, income from digitized businesses, which do not require physical presence of itself or agent in India.

Thereafter, the Finance Act, 2020 omitted the SEP provisions from A.Y.2021-22 and inserted new provision from A.Y.2022-23. The relevant extract of the Explanatory Memorandum of the Finance Bill, 2020 is as under -

*"Therefore, for the purposes of determining SEP of a non-resident in India, threshold for the aggregate amount of payments arising from the specified transactions and for the number of users were required to be prescribed in the Rules. However, since discussion on this issue is still going on in G20-OECD BEPS project, these numbers have not been notified yet. G20-OECD report is expected by the end of December 2020. In the circumstances, it is proposed to defer the applicability of SEP to starting from assessment year 2022-23.* ***Certain drafting changes have also been made while deferring the proposal.*** *The current SEP provisions shall be omitted from assessment year 2021-22 and the new provisions will take effect from 1st April, 2022 and will, accordingly, apply in relation to the assessment year 2022-23 and subsequent assessment years."*

Therefore, the drafting changes cannot have the effect of changing the intent

expressed in the Explanatory Memorandum to Finance Bill, 2018, namely, to bring within the fold of section 9, income from digitized businesses, which do not require physical presence of itself or agent in India.

**(b) Determination of income attributable to transactions and activities constituting SEP**

Further, as per the second proviso to Explanation 2A to section 9(1)(i), only the income attributable to transactions and activities which constitute significant economic presence shall be deemed to accrue or arise in India. However, the rules relating to determination of income attributable to such transactions and activities have not been notified.

**Suggestion**

It is suggested that -

(i) Explanation 2A to Section 9(1)(i) may be amended to ensure that the provisions related to significant economic presence are limited to digital commerce rather than commerce involving physical goods with traditional system of entering into contracts etc.

(ii) Till the rules relating to attribution of income component of the transactions and activities constituting SEP are in place, there should not be any obligation to deduct tax if such obligation to deduct tax arises only on account of application of SEP.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 107. Section 47 – Transactions which are not regarded as transfer – Exemption should also be available in case of amalgamation of an Indian company with a foreign company

### Provision of Law

As per Section 47(vi), any transfer, in a scheme of amalgamation, of a capital asset by the amalgamating company to the amalgamated company would not be regarded as transfer for capital gains purposes, if the amalgamated company is an Indian company.

### Issue

A transaction of amalgamation, where the amalgamated company is an Indian company, is exempt from capital gains tax liability. Further, in case of an inbound merger, the capital gains arising to the shareholders of the amalgamating company is also exempt. Similar tax exemption is, however, not available to the amalgamated company or its shareholders in case of an outbound merger.

Post an outbound merger, the assets, liabilities and employees of the amalgamating Indian company may continue to physically exist in India. This may create a PE exposure for the amalgamated foreign company. In that event, business profits attributable to the foreign amalgamated company's PE in India will be liable to tax at the rate of 40% (*plus* applicable surcharge and cess).

The merger of an Indian company with a foreign company in a specified jurisdiction is now permitted as per section 234 of the Companies Act, 2013 r.w. Rule 25A of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016. The FEMA Merger Rules have also been amended to permit an outbound merger, subject to conditions. One such condition is that a foreign company can acquire and hold only certain assets in India which are permitted under the relevant FEMA regulations for the acquisition of property in India.

Such cross-border mergers would not be attractive till the time there exists tax liability or ambiguity around taxability for such transactions. The income tax provisions, therefore, need to be aligned with corporate law and FEMA to achieve the objective of increasing the ease of winding up operations in India.

**Suggestions**

It is suggested that:

(i) the condition specified in section 47(vi) that the amalgamated entity should be an Indian company for claiming exemption from capital gains tax arising on transfer of the undertaking may be removed.

(ii) the shareholders of the Indian company receiving shares of the foreign amalgamated company should not be subject to capital gains.

(iii) the condition specified in section 2(1B) that all assets and liabilities of the undertaking should be transferred in amalgamation be relaxed since due to restrictions laid down in FEMA Regulations, it is not possible to transfer all assets and liabilities pertaining to the undertaking to the amalgamated foreign company.

(iv) Since post amalgamation, the foreign amalgamated company would carry on business in India, a specific provision may be added to the definition of 'business connection' u/s 9(1)(i) to bring clarity to future taxability of the foreign amalgamated entity.

(v) The carried forward business losses and unabsorbed depreciation of the amalgamating Indian entity may be available for set-off to the permanent establishment of the amalgamated foreign entity.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 108. Section 92C(2) and Rule 10CA – Construction of data set for determining ALP – Arm's length range to be aligned with global practices

### Provision of Law

Section 92C(1) requires determination of arm's length price by any of the methods mentioned therein, being the most appropriate method. Section 92C(2) provides that the most appropriate method referred to in section 92C(1) shall be applied, for determination of arm's length price, in the manner as may be prescribed. Accordingly, as per Rule 10CA(4), arm's length range beginning from the 35th percentile of the data set and ending on the 65th percentile of the dataset has to be constructed where the data set consists of six or more entries and the most appropriate method is a method other than profit split method or any other method as may be prescribed by the Board.

### Issue

Globally, arm's length range is the Inter quartile range (25th to 75th percentile of the dataset). This is the practice in most of the countries, for eg. US, Canada, UK, etc. There is a need for alignment with global practices, as the benchmarking from one country perspective can be applied from the other country perspective as well, which will also help reduce the compliance cost for the assessee.

### Suggestion

It is suggested that the arm's length range in India be aligned with the globally accepted inter quartile range of 25$^{th}$ to 75$^{th}$ percentile of the dataset.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 109. Section 92CE - Secondary Adjustment – Increase in threshold of primary adjustment and provision for reversal of advance

### Provisions of Law

Section 92CE(1) provides the different circumstances when primary adjustment to transfer price is made, where the assessee has to make a secondary adjustment. However, if the primary adjustment does not exceed Rs.1 crore, the assessee need not make secondary adjustment. This is contained in the proviso to section 92CE(1).

Section 92CE(2) provides that if the excess money available with the associated enterprise is not repatriated to India within the prescribed time, the same shall be deemed to be an advance made by the assessee to the associated enterprise, and the interest on such advance shall be computed in the prescribed manner.

### Issues

(a) Section 92CE provides for computation of interest income in pursuance of secondary adjustment, which is considered as deemed income. However, the same is not specifically included in the definition of income under section 2(24).

(b) As per section 92CE, as a consequence of a primary adjustment made to align the transfer price with the arm length price, certain secondary adjustments are required to be made for the purpose of correct allocation of cost and profit to the associated enterprises. Such adjustments are made when the value of primary adjustment exceeds Rs.1 crore. However, as per the FEMA Act, 1999 which provides for a liberalized remittance scheme (LRS) the amount of remittance that could be made to a resident individual abroad is upto $ 250000.

(c) Section 92CE deems the difference between the transaction price and arm's length price as an advance (which is to be recorded in the books) and provides for imputation of interest on such advances. However, there is no specific provision to reverse the advances appearing in the books even in case where the Associated Enterprise relationship ceases to exist or in case where the excess money is repatriated.

**Suggestion**

It is suggested that -

(a) interest income pursuant to secondary adjustments under section 92CE may be included in the definition of income under section 2(24).

(b) in order to align the income-tax law with FEMA, the threshold limit for subjecting a transaction to secondary adjustment may be increased from Rs.1 crore to Rs.2 crore

(c) it may be specifically provided that the advances appearing in the books of the parties be reversed in cases where AE relationship ceases to exist, or excess money is repatriated.

***(SUGGESTION FOR REDUCING/MINIMIZING LITIGATIONS)***

## 110. Section 94A – Withholding tax@30% in case of payments to persons located in notified jurisdictional area (NJA)– Section 94A to prevail over section 206AA

### Provisions of Law

One of the tax consequences of a country or area being notified as NJA is that payments to persons located in that NJA would be subject to a higher withholding @ 30%. The relevant provision which provides for this implication i.e., section 94A(5), would be applicable notwithstanding anything to the contrary contained in the Act.

Section 206AA which provides for higher withholding @ 20% in absence of PAN of payee is also applicable not withstanding anything to the contrary contained in the Act.

### Issue

Though the intent appears to be that section 94A would override section 206AA, there may be some difficulties in interpretation.

### Suggestion

Section 94A and/or section 206AA may be suitably amended to clarify that section 94A would prevail in case tax is to be deducted with respect to any payment to a person located in a NJA.

***(SUGGESTION FOR MINIMIZING LITIGATION)***

## 111. Section 94B - Limitation of interest benefit provisions – Clarification on the manner of computation of excess interest and the concern arising on account of the deeming provision where an associate provides a guarantee to the lender

### Provision of Law

Section 94B deals with limitation on interest deduction in certain cases. Sub-sections (1) and (2) thereof read as under:

"94B. *(1) Notwithstanding anything contained in this Act, where an Indian company, or a permanent establishment of a foreign company in India, being the borrower, incurs any expenditure by way of interest or of similar nature exceeding one crore rupees which is deductible in computing income chargeable under the head "Profits and gains of business or profession" in respect of any debt issued by a non-resident, being an associated enterprise of such borrower, the interest shall not be deductible in computation of income under the said head to the extent that it arises from excess interest, as specified in sub-section (2):*

***Provided*** *that where the debt is issued by a lender which is not associated but an associated enterprise either provides an implicit or explicit guarantee to such lender or deposits a corresponding and matching amount of funds with the lender, such debt shall be deemed to have been issued by an associated enterprise.*

*(1A) Nothing contained in sub-section (1) shall apply to interest paid in respect of a debt issued by a lender which is a permanent establishment in India of a non-resident, being a person engaged in the business of banking.*

*(2) For the purposes of sub-section (1),* ***the excess interest shall mean an amount of total interest paid or payable in excess of thirty per cent of earnings before interest, taxes, depreciation and amortisation of the borrower in the previous year or interest paid or payable to associated enterprises for that previous year, whichever is less."(emphasis supplied)****.*

### Issue

### (a) Manner of computation of excess interest

Section 94B(2) refers to "*an amount of total interest paid or payable*". The literal reading of the section does not create any limitation on inclusion of interest paid or payable to associated enterprises only. The words referred to are 'total interest paid or payable'. The legislature has separately referred to "*an amount of total interest paid or payable*" and "*interest paid or payable to associated enterprises*" within the same sub-section itself. Thus, on the basis a plain reading of section 94B(2), interest paid to third party lenders would be

includible in 'total interest paid or payable' for the purposes of computing the excess interest under section 94B(2).

Whereas section 94B(2) defines excess interest as the total interest payable in excess of 30% of EBITDA, section 94B(1) read with the Explanatory Memorandum to the Finance Bill, 2017, indicates that the disallowance is in relation to interest in respect of debt issued by a non-resident associated enterprise of the borrower. The issue under consideration is whether for purpose of determining the amount of excess interest under section 94B(2), interest paid to third party lenders (i.e. other than associated enterprises) should be included in 'total interest paid or payable' or it should only include interest paid or payable to associated enterprises.

**(b) Applicability in cases where borrowings are secured on the basis of guarantee given by non-resident associated enterprises**

As per FDI Policy, 100% FDI towards infrastructure falls under automatic route. Foreign investors invest in India with combination of equity and debt. Further maximum debt is backed by parent guarantee. The parent guarantee helps Indian borrowers to reduce the interest rate on their borrowing. Given high capital intensive nature of the infrastructure sector, reduced interest costs makes the project further viable.

Disallowance / limitation of allowance of interest expense on instances where such borrowing is secured by guarantee of associated enterprise will adversely affect the viability of infrastructure projects.

**(c) Applicability of section 94B to lending by Indian banks to Indian enterprises on the basis of guarantee given by non-resident associated enterprises**

On a plain reading of the proviso to section 94B(1), it appears that if an Indian bank lends to an Indian enterprise on the basis of guarantee given by a non-resident associated enterprise, interest on such loan will attract the provisions of section 94B. It may be noted that section 94B(1A) provides that the limitation of interest deduction will not apply, to interest paid in respect of a debt issued by a lender which is a PE in India of a non-resident, being a person engaged in the business of banking.

Thus, on a combined reading of the proviso to section 94B(1) and section 94B(1A) it appears that whereas a PE of a foreign bank is excluded from applicability of the limitation of interest deduction, an Indian bank will be subject to limitation of interest deduction, if it gives a loan on the basis of guarantee of a non-resident associated enterprise. However, this does not appear to be the legislative intent.

**Suggestion**

It is suggested that –

(a) for the purpose of computing 'excess interest' under section 94B(2), the term 'total interest paid or payable' should only include interest paid to the associated enterprises.

(b) borrowings by Indian companies backed by corporate guarantee may be excluded from applicability of section 94B.

(c) loan taken from an Indian bank which is guaranteed by a non-resident associated enterprise should be excluded from the scope of section 94B.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 112. Section 97(1) read with Rule 10U – Threshold tax benefit of Rs.3 crore for applicability of GAAR provisions – Need for increase in threshold and clarification of meaning of tax benefit

### Provision of Law

Section 97(1) provides that an arrangement shall be deemed to be lacking commercial substance, if inter alia; -

- it involves the location of an asset or of a transaction or of the place of residence of any party which is without any substantial commercial purpose other than obtaining a tax benefit for a party; or
- it does not have a significant effect upon business risks, or net cash flows apart from the tax benefit.

As per section 102(10), "tax benefit" includes, —

(a) a reduction or avoidance or deferral of tax or other amount payable under this Act; or

(b) an increase in a refund of tax or other amount under this Act; or

(c) a reduction or avoidance or deferral of tax or other amount that would be payable under this Act, as a result of a tax treaty; or

(d) an increase in a refund of tax or other amount under this Act as a result of a tax treaty; or

(e) a reduction in total income; or

(f) an increase in loss,

in the relevant previous year or any other previous year;" (Emphasis supplied)

As per Rule 10U of the Income-tax Rules, 1962, certain arrangements are excluded from the provisions of Chapter X-A. An arrangement where the tax benefit in the relevant assessment year arising, in aggregate, to all the parties to the arrangement does not exceed a sum of rupees three crore is excluded from the applicability of the provisions of Chapter X-A.

### Issue

(i) Sub-clauses (e) and (f) in the definition refer to "reduction of total income" and "increase in loss" as tax benefit. An ambiguity arises as to how tax benefit is conditioned at income / loss level. This may also defeat the objective of Rs.3 crore tax benefit threshold as provided in Rule 10U of the Income-tax Rules, 1962 (the Rules).

Computation of tax benefit on deferral of tax (which is merely a timing difference) needs to be clarified. As observed by the Expert Committee recommendations[1], in cases of tax deferral, the only benefit to the taxpayer is not paying taxes in one year but paying it in a later year. Overall, there may not be any tax benefit but the benefit is in terms of the present value of money.

(ii) Further, as observed by the Expert Committee[2], the term tax benefit has been defined to include tax or other amount payable under this Act or reduction in income or increase in loss. The other amount could cover interest.

(iii) the threshold of tax benefit of Rs. 3 crore for application of GAAR provisions is low. Globally, similar anti-avoidance measures are attracted with higher thresholds, and raising the limit will help align Indian provisions with international tax practices, and also ensure that efforts are directed to cases where there is large-scale tax avoidance.

**Suggestion**

It is suggested that -

(i) Sub-clauses (e) and (f) may be appropriately worded to correspond with the 'tax' amount. In other words, the reference to income/loss should not be the base for defining the term 'tax benefit'.

(ii) Further, for the sake of clarity, it may be specified that tax benefit for the purposes of the threshold shall include only income tax and shall not include other amounts like interest, etc.

(iii) the threshold limit for attracting GAAR provisions be increased from Rs. 3 crore to Rs. 10 crore in Rule 10U - Chapter X-A not to apply in certain cases. This will ensure that the efforts are directed on the high value transactions.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

[1]Page 48 and 49 of the Final Report by the Expert Committee on GAAR chaired by Dr. Parthasarathi Shome.
[2]Page 47 of the Final Report by the Expert Committee on GAAR chaired by Dr. Parthasarathi Shome.

## 113. Section 194LC - Income by way of interest from Indian Company – Modification in language of law in section 194LC(2)(ii) to convey the true intent

### Provision of Law

Section 194LC provides that the interest income payable by a specified company or a business trust to a non-resident shall be subjected to tax deduction at source at the rate of 5%. Section 115A provides that such income will be taxed at the rate of 5%.

Section 194LC(2)(ii) provides that for the purpose of deduction of tax at source at the rate of 5%, the interest payable by a specified company or a business trust to a non-resident, not being a company or a foreign company, shall be the income payable by the specified company or a business trust **to the extent to which such interest does not exceed** the amount of interest calculated at the rate approved by the Central Government in this regard, having regard to the terms of the loan or the bond and its repayment.

### Issue

It is imperative to note that the phrase "To the extent to which such interest does not exceed" may be interpreted to mean that in case the borrowings are made at a rate higher than the rate approved by the Central Government, the excess interest income (over and above the interest calculated at the approved rate) will be subject to tax at the rate of 20%. As per the Explanatory Memorandum to the Finance Bill, 2012, this amendment was made in order to augment long-term low-cost funds from abroad. It is felt that such wording may be inadvertent and hence, needs to be reworded.

### Suggestion

In order to bring out the real intent of the law, it is suggested that section 194LC(2)(ii) may be reworded to provide that the interest referred to in sub-section (1) shall be the income by way of interest payable by the specified company or business trust "IF such interest does not exceed the amount of interest calculated at the rate approved by the Central Government in this regard, having regard to the terms of the loan or the bond and its repayment".

***(SUGGESTION FOR MINIMIZING/REDUCING LITIGATION)***

## 114. Section 195 –Tax deduction by any person responsible for paying to a non-corporate non-resident or a foreign company – Certain concerns to be addressed

### (a) Time limit to be prescribed for determination by the Assessing Officer of appropriate portion of the sum so chargeable

**Provision of Law**

Section 195(2) provides that where the person responsible for paying any such sum chargeable under the Act to a non-resident considers that the whole of such sum would not be income chargeable in the case of a recipient, he may make an application to the Assessing Officer in the prescribed form and manner to determine the appropriate portion of the sum so chargeable and upon such determination, tax shall be deducted only on that proportion of the sum which is so chargeable.

**Issue**

It may be noted that no time limit for such determination has been prescribed in the Act, which causes undue hardship in genuine cases.

**Suggestion**

It is suggested that an appropriate time limit say thirty (30) days may be prescribed for such determination by the Assessing officer.

### (b) Relaxation of penalty under section 271-I for non-furnishing of information u/s 195(6)

**Provision of Law**

A penalty of Rs.1 lakh is leviable under section 271-I for failure to furnish information or for furnishing inaccurate information under section 195(6).

**Issue**

The penalty is quite high, considering that the reporting requirement may be in relation to a transaction which is not chargeable to tax.

**Suggestion**

The penalty may be reduced, in case non-furnishing of information relates to a transaction not chargeable to tax.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## (c) TCS on international credit card payments

**Issue**

Resident individuals often use their credit cards to pay foreign entities for goods purchased / services availed in foreign currency. Whenever a credit card transaction is made in a foreign currency, a fee is charged from customers to process such transaction.

Currently, the authorised persons referred to in section 2(c) of the FEMA Act, 1999 are required to report in the statement of financial transaction, if the expenditure in foreign currency of any person, by way of inter alia, credit card or debit card is Rs.10 lakh or more in aggregate in a financial year. Also, banks are required to report in the SFT, credit card payments of Rs.1 lakh or more in cash or Rs.10 lakh or more by any other mode by a person in a financial year.

In order to further strengthen the mechanism to capture foreign currency transactions through credit card, TCS provisions may be introduced.

**Suggestion**

It is suggested that tax be collected on foreign currency transactions through credit cards, so that all such transactions can be captured.

***(SUGGESTION FOR IMPROVING TAX COLLECTION)***

## 115. Section 204 – "Person responsible for paying" – Removal of Reference to section 285 & Incorporation of meaning of "Person responsible for collecting"

### Provision of Law

In section 204, the "person responsible for paying" has been defined for the purposes of the foregoing provisions of Chapter XVII and section 285.

### Issues

(a) Since section 285 is in respect of submission of statement by a non-resident having liaison office, the definition of "person responsible for paying" given in section 204 is not relevant in the context of section 285.

(b) While the meaning of "person responsible for paying" has been defined under the Act, "person responsible for collecting" has not been defined anywhere in the Act.

### Suggestion

It is suggested that -

(a) Section 204 may be amended to remove reference to section 285.

(b) The meaning of "person responsible for collecting" may be incorporated in the Act for clarity.

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

## 116. Section 197 – Application for non-deduction of tax at source or deduction of tax at a lower rate – Requirement to obtain certificate from Assessing Officer – Concerns in case of tax deduction by a resident on payment made to a non-resident for purchase of residential property - Report from Chartered Accountant certifying sum chargeable to tax and exemption to the transferee from requirement of obtaining TAN

### Provision of Law

Section 197(1) requires the assessee to file an application to the Assessing Officer for deduction of tax at a lower rate or non-deduction of tax under, *inter alia*, section 195. On such application, the Assessing Officer may give to him, such certificate as may be appropriate.

Section 195 requires any person responsible for paying to a non-resident, not being a company, or to a foreign company, any interest (not being interest referred to in section 194LB or section 194LC or section 194LD) or **any other sum chargeable under the provisions of this Act** (not being income chargeable under the head "Salaries") shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax thereon at the rates in force.

### Issue

When a non-resident transfers residential property to a resident, tax has to be withheld by the resident transferee of immovable property at the rate of 12.5% *plus* applicable surcharge and cess in case of long-term capital asset and 30% *plus* applicable surcharge and cess in case of short-term capital asset.

There may be a situation for the non-resident transferor that the tax incidence on capital gain is lower or nil. In case non-resident transferor estimates a lower tax liability or nil tax liability, he/she may approach to his/her jurisdictional Assessing officer by filing Form 13 under section 197 of the Income-tax Act, 1961.

The transferee has to obtain a tax deduction and collection account number (TAN). In case the transferor is an NRI, it takes at least 7 to 10 working days to have it activated. It may take at least 30 days to put up the Form 13 to the approving authority. Practically, the procedure takes not less than 45 days to have the Lower Deduction Certificate. This causes genuine hardship for both buyer and seller.

Further, if the transferee is not carrying on business or profession and he is not required to deduct tax generally, then, he has to obtain TAN only for this transaction. In addition to the above-mentioned points, the non-resident has to

create login for making application for lower deduction certificate. The login can be created after validation. For the validation, the following are required -

*Details of TDS/TCS Deposited.* – This is generally not available with the deductee because earlier he was not required to deposit tax.

*Challan Details of Tax Deposited by Taxpayer* - This is also generally not available with the deductee.

*Mention Details of 26QB statement details filed by Buyer before correction* – This is also generally not available with the deductee. This is required for compliance u/s 194-IA, this is applicable when the transferor is resident.

*Authentication through Aadhaar / VID* - The non-resident is not required to have a Aadhar number.

This causes genuine hardship for the deductee to register himself with the TRACES portal to make application for lower deduction certificate.

**In this context, it may be noted that in *Transmission Corporation of A.P. Ltd. vs. Commissioner of Income Tax (1999) 239 ITR 587*, the Supreme Court has held that the obligation of the assessee to deduct tax at source under section 195 is limited only to the appropriate proportion of income chargeable under the Act. Accordingly, the deductee may not be made to undergo such a cumbersome process for obtaining lower tax deduction certificate, if tax at the applicable rate is deducted on the sum chargeable to tax and not the entire consideration.**

**Also, drawing a parallel reference to section 194-IA (which applies to resident transferors), where a transferee responsible for paying to a resident transferor any sum by way of consideration for transfer of any immovable property is required to deduct tax@1% on actual consideration or stamp duty value of the property, whichever is higher, without the requirement to obtain a TAN. A similar provision may be introduced where a transferee is responsible for paying to a non-resident transferor any sum by way of consideration for transfer of any immovable property. In such cases, the resident transferee may be allowed to deduct tax at source on payments made to a non-resident seller at the applicable rate without obtaining a TAN.**

**Suggestion**

It is suggested that -

(i) Considering the decision of the Supreme Court in *Transmission Corporation of A.P. Ltd.'* s case (supra), **a report of a chartered accountant in the prescribed form certifying the sum chargeable to tax be obtained**. Tax@12.5% would be deductible where the sum chargeable to tax represents capital gains on transfer of a long-term capital asset and tax@ 30% would be deductible where the sum chargeable to tax represents capital gains from transfer of a short-term capital asset. This would alleviate the requirement of having to obtain certificate for lower deduction of tax at source.

(ii) **The transferee responsible for paying to a non-resident transferor may be exempted from the requirement to obtain TAN.**

***(SUGGESTION FOR RATIONALIZATION OF PROVISIONS OF DIRECT TAX LAWS)***

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***(Set up by an Act of Parliament)***
**ICAI BHAWAN Sixth Floor, Hostel Block A-29, Sector - 62, NOIDA (U.P.), India**
**Email: dtc@icai.in and dtc.int@icai.in Website: www.icai.org**