

PricewaterhouseCoopers  
Direct Tax Code 2009 – Uncoded  
August 2009

## Backdrop

- Current law – Income-tax Act, 1961
- Almost five decades old
- Over 5000 amendments – seriously mutilated!
- New Code in the making for four years

## Stated objectives

- Simplicity
- Minimising litigation
- Broadbasing the tax base
- Eliminating exemptions

# Commencement

- Applicability – Financial year 1st April 2010
  - Confusing indications for later applicability

# International Tax

## Taxation of Non-resident companies

	Existing (%)	Proposed (%)
Corporate tax	42.23	25
Branch Profits Tax	-	15
MAT	16.995	2 / 0.25 on assets
Capital gains tax	varying	30
Royalty/Fees for Technical Services	10.56	20

## General Anti-avoidance Rules

- General Anti-avoidance Rules (“GAAR”) introduced
- Sweeping discretionary powers to treat an arrangement impermissible
- Impermissible arrangements may be disregarded or re-characterised
- Onus on taxpayer to demonstrate purpose of the arrangement
  - obtaining tax benefit should not be the main purpose

## Treaty Override

- For determining relationship between a treaty and the Code
  - No preferential status to either
  - Whichever is later in point of time, to prevail
- Rule of 'more beneficial' of Act or treaty no longer applicable?
- Existing treaties continue in force

## Branch Profit tax

- Branch profits tax introduced on foreign companies at 15% on net-of-tax profits
- No direct reference to a branch
  - Apply to all income?
  - Apply only where branch exists?
  - Apply only to branch income?
- Branch not defined
  - Project Office?
  - Permanent Establishment without ground presence?
- Not linked to repatriation

## Other significant changes

- Foreign company may be treated as a resident in India if its control and management is situated even partly in India
  - Currently control and management to be wholly in India
- Income from indirect transfer of any capital asset situate in India to be taxable
- Interest paid by a non-resident for earning any income from any source in India to be taxable

## Non-residents – Other issues

- Business connection to be formed through independent agent as well
- Definition of royalty expanded
  - Transfer of all or any rights in respect of
    - live coverage of any event
    - Cinematographic films
  - Rights relating to transmission by satellite, cable, optic fibre, etc
- Deduction of head office expenses
  - Allowable up to 0.5 % of sales turnover
  - Currently based on taxable income

# Transfer Pricing

- Introduction of Advance Pricing Agreements (APA)
- For an APA, arm's length price to be determined based on Indian transfer pricing provisions
- APA decision is binding upon tax authority and tax payer
- Validity of APA decision – not exceeding five consecutive years
- Transfer pricing penalties eased
- Definition of Associated Enterprises widened
  - Amongst others, shareholding relationship of 10% sufficient to create association amongst enterprises

# Corporate taxation

## Taxation of resident companies

	Existing (%)	Proposed (%)
Corporate tax	33.99	25
Dividend Distribution Tax	16.995	15
MAT	16.995	2 / 0.25 on assets
Capital gains tax	varying	25

## General

- Corporate Tax Rate reduced to 25%
- Dividend distribution tax reduced
- MAT – transition from ‘book profit’ to ‘value of gross assets’
- Unlimited carry forward of losses
- Distinction between normal and speculation profits retained

## Business Income – Computation Methodology

Particulars	Amount (Rs)	Amount (Rs)
Gross Earnings		XXX
Less: Business Expenditure		
Operating Expenditure	XX	
Permitted Finance Charges	XX	
Capital Allowances	XX	XXX
Taxable income from Business		XXX

- Income from each business to be aggregated
  - Except income for which specific income computation rules apply (like Infrastructure, SEZ developers, Power, etc.)
  - Loss from such business not to be set off against profits from other businesses

# Computation

- Gross Earnings to also cover
  - Reduction, remission or cessation of any liability by way of loan, deposit, advance or trade credit
  - Amount accrued or received on account of cessation, termination, etc, of any agreement entered in the course of business
- Profit on sale of business capital assets or on slump sale to be taxed as business income and not capital gains

## Deferred revenue expenditure

- Specific Deferred revenue expenditure eligible for capital allowance

Block of Assets	Depreciation Rate (%)
Non-compete fees	25
Premium on obtaining assets on lease / rent	25
VRS expenditure	25
Business re-organisation expenditure	25
Expenditure on prospecting mineral or development of mine / other natural deposit of any mineral	15

## Capital Allowances

- 150% weighted deduction for in-house scientific R&D expenditure; extended to all industries
- Loss upon sale of entire block of assets to be ignored
  - Depreciation on block to continue
- Lessee eligible to claim capital allowance in case of finance lease

## Minimum Alternative Tax ('MAT')

- Payable by company on 'value of gross assets' instead of on 'book profits'
- Tax Rate
  - Banking Company – 0.25%
  - Other Company – 2%
- Computation of value of gross asset
  - Value of gross block of fixed asset less accumulated depreciation
  - Capital work in progress
  - Book value of other assets (investments, current assets, etc.)
- No tax credit / set off allowed in subsequent years
- Multiple level taxation – holding-subsidiary structures

## Dividend Distribution Tax

- Status quo on Dividend Distribution Tax ('DDT') rate @ 15%
- DDT extended to all dividends
- Dividend distributed to following pass-through entities exempt from DDT
  - New pension trust scheme
  - Mutual Funds (including venture capital vehicles)
  - Approved provident and superannuation funds
  - Life Insurance Companies
- DDT exemption for SEZ developers discontinued

## Losses of closely-held companies

- Widely-held companies to include all public companies - listed or unlisted
- No distinction between unabsorbed depreciation and loss
- Capital losses may be carried forward even after change in ownership

## Tax Deduction at Source

- TDS on payments of Goods?
- No lower rate deduction?
- No time limit for completion of assessment of TDS/TCS Returns
  - Time limits were recently introduced

# Tax incentives

## General

- Profit-based tax incentives sought to be discontinued
- Expenditure / Investment-based incentive scheme introduced
- Large Infrastructure Projects including development of Special Economic Zones (“SEZ”) under new scheme
- Export-based Incentives such as for units in Software Technology Parks or SEZs to be discontinued
- Grandfathering referred to in Discussion Paper
  - Only a few provisions grand-fathered in the Code

## Eligibility for new incentives

- Generation, transmission or distribution of power
- Developing or operating/maintaining Infrastructure facilities
  - Roads including toll roads, bridges or rail systems
  - Highway projects including housing or other activities which are an integral part of a highway system
  - Water supply projects, water treatment systems, irrigation projects, sanitation and sewerage systems, solid waste management system; and
  - Ports, airports, inland waterways, inland ports

## Eligibility for new incentives – Continued

- Operating and maintaining hospitals in specified areas
- Processing, preservation and packaging of fruits and vegetables
- Laying and operating cross-country natural gas / crude / petroleum pipeline distribution network, including storage facilities
- Setting up and operating cold chain facilities
- Setting up and operating agricultural warehousing facilities
- Exploration and production of mineral oil or natural gas
- Developing SEZs

## Investment-based deductions

- Allowable deductions include
  - Expenditure on purchase, lease or rental of land or land rights
  - Capital expenditure on most assets
  - Expenditure incurred before commencement of business
- Eligible business to be treated as separate business

# Capital Gains

## General

- Distinction between long-term and short-term gains removed
- Capital gains taxable at normal rates for residents
- Capital gains taxable at 30% for non-residents
- Gains on transfer of business capital assets to be taxable as business income
- Other capital assets referred to as 'Investment Assets'
- Securities Transaction Tax proposed to be abolished

## Deduction of tax at source

- Tax to be deducted on capital gains
  - From payments to residents @ 10%
  - From payments to non-Residents, including FIIs @ 30%
- On subsequent transfer, no allowance for cost of acquisition, if tax not deducted

## Other issues

- Exemption in respect of transfer of investment asset in a transaction of reverse mortgage not provided
- No transitional provisions dealing with transfers before commencement
- Indexation available only for assets held for one full financial year
- Indexation benefit now available for bonds and debentures also
- Indexation benefits available to non-residents also
  - Adjustment for exchange fluctuation no longer available
- Substitution of cost by fair market value
  - Base date shifted from 1.4.1981 to 1.4.2000

## Other issues – Continued

- Cost of acquisition of asset deemed to be nil if not determinable
- No provision for cost determination and period of holding in case of dematerialised shares
  - “FIFO” prescribed under existing provisions

# Roll-over

- Roll-over available for re-investment of sale proceeds
- Roll-over available only to individuals/HUFs
- Investment to be made in new asset within
  - one year before or
  - three years from the end of the financial year in which transfer took place
- New asset to be acquired within the same financial year
  - Otherwise, sale proceeds to be deposited in Capital Gains Deposit Scheme
    - Amount to be withdrawn only for Investment in new asset
    - If not invested within one month of withdrawal, taxable in year of withdrawal
- If deposit not used within three years, exempted gains taxable in fourth year

## Roll-over – Continued

- No lock-in period for new asset acquired
- Qualifying new assets
  - Agricultural land – in case of gain on transfer of agricultural land
  - Residential house – in case of gain on transfer of any asset
  - Deposit in Capital Gains Saving Scheme (CGSS) – in case of gain on transfer of any asset
- Any withdrawal from CGSS is liable to tax under the head income from residuary sources in the year of withdrawal

## Set-off and carry forward of losses

- No distinction between long term and short term capital losses
- Capital losses not to be set off against any other income
- Capital losses allowed to be carried forward indefinitely
- Losses lapse if return not filed by due date
  - Applies even if no capital loss incurred in current year

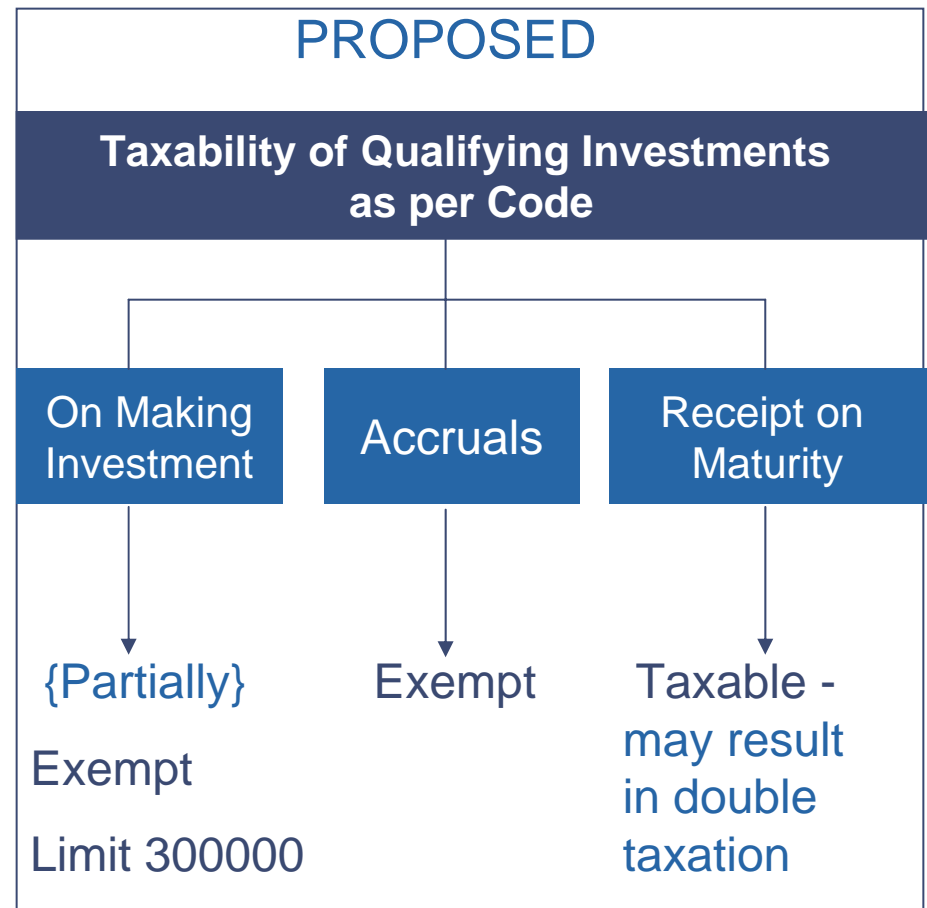
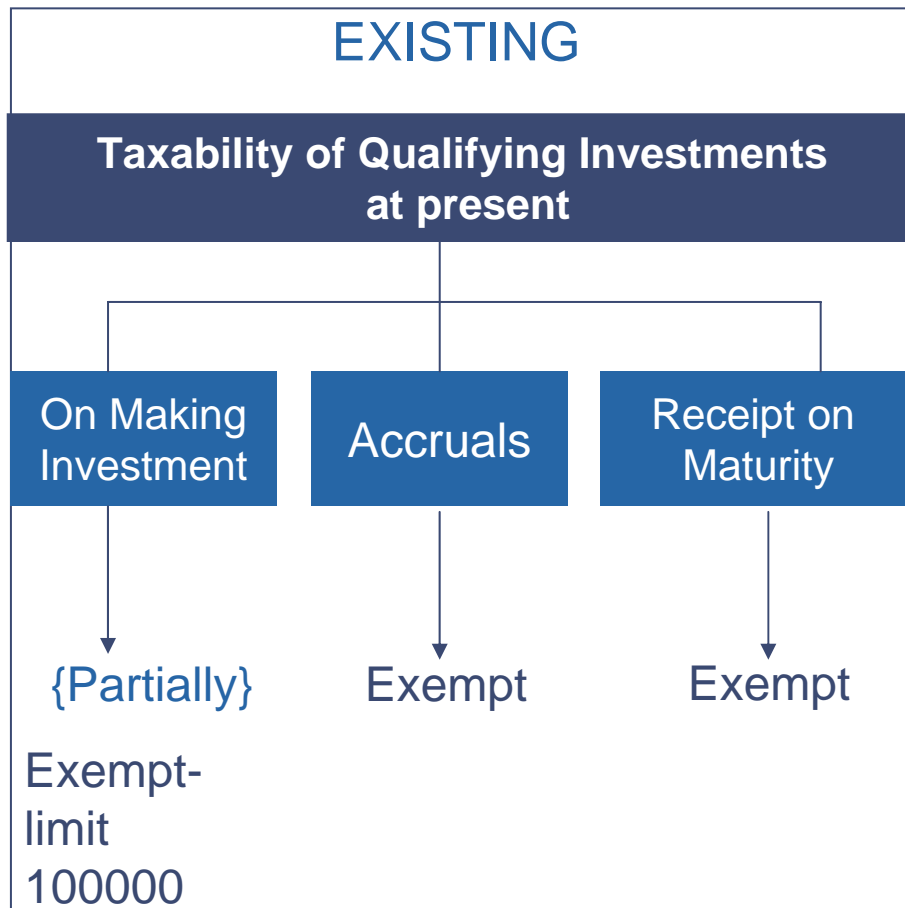
# Personal Taxation

## Tax rates for an individuals

Existing Income Slab (INR)	Tax Rate*	Proposed Income Slab (INR)	Tax Rate
Up to 1,60,000	Nil	Up to 1,60,000	Nil
1,60,001 to 3,00,000	10%	1,60,001 to 10,00,000	10%
3,00,001 to 5,00,000	20%	10,00,001 to 25,00,000	20%
Above 5,00,000	30%	Above 25,00,000	30%

\*Currently education cess is levied at 3% of the tax amount.

# Introduction of withdrawal-based taxation for investments



## Additional elements taxable

- House Rent Allowance
- The value of leave travel concession
- Medical reimbursement
- The value of free or concessional medical treatment
- The amount received on encashment of unavailed earned leave on retirement

## Deductions for savings

- Restricted to maximum of Rs. 300000 per year
- Amount deposited in accounts with permitted intermediaries
- Withdrawals not taxable if rolled over into another account
- Withdrawals from such accounts taxable

## Wealth Tax

- Individuals, HUFs and Private Discretionary Trusts liable to wealth tax
- Wealth tax abolished for companies
- Rate of wealth tax reduced from 1% to 0.25%
- Exemption limit enhanced from Rs. 30 Lakhs to Rs. 50 Crores
- All assets located in India or abroad liable to wealth tax, inter alia, except
  - Assets located outside India belonging to a non-resident or non-citizen
  - House or plot of land acquired or constructed before April 1, 2000

# Thank you