

# Budget Connect 2016

Highlights and impact of Indian  
Union Budget

# Direct taxes

## General

### Tax rates

- ▶ No changes in corporate tax rate with the exception of:
  - ▶ Domestic companies having turnover not exceeding INR 5 crores in the financial year 2014-15, the corporate tax rate has been reduced from 30% to 29% (plus surcharge and cess as applicable)
  - ▶ Domestic companies engaged in the manufacture of product or thing, setup after 1 March 2016, have the option of being taxed at 25% (plus surcharge and cess as applicable) subject to not claiming certain benefits / exemptions

## Tax incentives

### Incentive for employment generation

- ▶ Additional deduction of 30% for remuneration paid to new eligible employees extended to all sectors subject to fulfilment of prescribed conditions

### Phase out of incentives

- ▶ No profit linked deductions for infrastructure facilities, development of SEZ, production of Oil & Gas commencing on or after 1 April 2017
- ▶ Deduction on capital expenditure in respect of cold chain, warehousing, etc. restricted from 150% to 100% from 1 April 2017 onwards
- ▶ No deduction to be available to SEZ units commencing manufacture, production or provision of services on or after 1 April 2020
- ▶ Weighted deduction for skilled development expenditure to be reduced from existing 150% to 100% from 1 April 2020

- ▶ Weighted deduction for in-house scientific research restricted from 200% to 150% from 1 April 2017 to 31 March 2020 and to 100% from 1 April 2020
- ▶ The maximum tax depreciation rate has been capped at 40% with effect from 1 April 2017 (instead of the accelerated depreciation available upto 100%)

### Tax incentives for start-ups

- ▶ 100% profit deduction for eligible start-ups engaged in business involving innovation development, deployment or commercialisation of new products, processes or services driven by technology or intellectual property
- ▶ Deduction available for a period of 3 consecutive years out of the first 5 years
- ▶ For individuals/ HUF, willing to setup a start-up by selling a residential property to invest in the shares of such company, long term capital gains arising on account of transfer of a residential property shall not be charged to tax subject to fulfilment of prescribed conditions

### Incentive for patent exploitation

- ▶ Income derived by an Indian resident from exploitation of patent developed and registered in India to be subjected to beneficial tax rate of 10% (plus applicable surcharge and cess) on gross basis.

### Expenditure pertaining to exempt income

- ▶ Rationalising of provisions pertaining to disallowance of expenditure relating to exempt income where such disallowance would be lower of:
  - ▶ 1% of average of monthly value of investments yielding exempt income; or
  - ▶ actual expenditure claimed

### Capital gains tax on sale of shares

- ▶ The period of holding shares of unlisted companies for claiming long term capital gains benefit proposed to be reduced from 3 years to 2 years

- ▶ Clarification that long term capital gains to a non-resident on sale of shares of a private limited company to be taxed at 10% (plus surcharge and cess as applicable)

### Permanent Account Number ('PAN') requirements for non-residents

- ▶ Higher withholding tax rate applicable to non-residents for non-furnishing of PAN relaxed subject to certain conditions as may be prescribed

### Relief from levy of Minimum Alternate Tax ('MAT') to foreign companies

Clarification issued specifically providing that MAT would not be applicable to foreign companies, retrospectively from 1 April 2000, if such foreign company:

- ▶ Is located in a country/ jurisdiction with which India has entered into a Double Taxation Avoidance Agreement ('DTAA') and such company does not have a Permanent Establishment ('PE') in Indian
- ▶ Is located in a country/ jurisdiction with which India does not have a DTAA and is also not required to seek registration under any law for the time being in force relating to companies.

## Base Erosion and Profit Shifting ('BEPS') agenda

### Tax levy on online advertising

- ▶ A new equalization levy is proposed to be introduced on payments made to non-resident entities not having a PE in India for online advertisement services, advertisement space, or any other facility or service for the purpose of online advertisement
- ▶ From a prescribed date (to be notified later), a taxpayer engaged in business or profession making the above payment to a non-resident entity shall be required to withhold 6% of the consideration paid for

such services where the amount of payment exceeds INR 100,000 in a financial year

### Place of Effective Management ('POEM') provisions

- ▶ The applicability of POEM provisions for tax residency of foreign companies deferred by one year i.e. 1 April 2017
- ▶ Transitional provisions to be prescribed for foreign companies determined to be Indian residents under the POEM provisions

### Country by Country Reporting ('CBCR') for transfer pricing

- ▶ In line with the recommendations contained in OECD Action Plan 13, enhanced transfer pricing documentation requirements including 'Master file' and 'Country by Country Reporting' have been introduced with effect from financial year 2016-17. The rules apply to international groups having consolidated annual turnover in excess of Euro 750mn (~INR 5.4bn)
- ▶ While the master file needs to be maintained by every group entity and filed locally with the tax authorities, the CBCR report generally needs to be filed by the parent entity of the group with the tax authority of its jurisdiction; however, in certain instances, the CBCR report may also need to be filed by the Indian subsidiary with the Indian tax authorities. Detailed documentation rules are yet to be notified

## Anti-avoidance

### General Anti Avoidance Rules ('GAAR')

- ▶ Government committed to implementing GAAR from 1 April 2017

### Buy-back tax provisions

- ▶ Scope of buy-back distribution tax has been enhanced to include all buy-backs of unlisted shares undertaken in accordance with any law relating to companies for the time being in force

## Tax administration

- ▶ Tax officers required to mandatorily make summary assessment, by processing the return of income, before making scrutiny assessment order
- ▶ Scope of summary assessment widened to include:
  - ▶ Disallowance of loss claimed, if return of income filing is delayed
  - ▶ Disallowance of expenditure indicated in tax audit report but not considered in the return of income
  - ▶ Disallowance of profit linked deduction claimed, if the return filing is delayed
  - ▶ Addition of income appearing in Form 26AS or Form 16A or Form 16 which has not been included in the return of income

Necessary provisions introduced to provide opportunity of being heard to the taxpayer before making the above adjustments

- ▶ Instruction to be issued to field officers to grant stay of tax demand if the taxpayer pays 15% of the disputed demand, pending appeal before the Commissioner of Income Tax (Appeals) ('CIT(A)')
- ▶ Penalty to be limited to 50% of the tax evaded; however in a case of misreporting of income, the penalty shall be 200% of the tax evaded
- ▶ With effect from 1 June 2016, the tax department shall not be allowed to appeal against the order of the Dispute Resolution Panel
- ▶ Time limit for passing order giving effect to order of CIT(A) / Tribunal has been fixed at 3 months (extendable by another 3 months with prior approval of Commissioner) from the receipt of the order. In case of failure to pass the order within such time-limit, the tax department would be required to pay interest at the rate of 9% per annum instead of 6% per annum

# Indirect Taxes

## Service tax

- ▶ No increase in service tax rate
- ▶ Krishi Kalyan Cess at 0.50% of value of all taxable services introduced on all taxable services (wef 1 June 2016). This will increase effective service tax rate to 15 percent (including 0.5% Swachh Bharat Cess). The CENVAT credit of such cess would be allowed to be used against output cess liability.
- ▶ No change in Swachh Bharat Cess ('SBC'). Thus SBC continues to be non-creditable.

### A. Ocean / Air freight

#### Inbound cargo

- ▶ Currently, services by way of transport of goods by an aircraft or vessel from a place outside India to a customs station of clearance in India is covered by negative list and hence outside the service tax net.

It is proposed that such services by way of transport of goods by a vessel would now be subject to service tax (wef 1 June 2016). The key impact of this proposal will be:

- ▶ Domestic shipping companies would charge service tax for inbound ocean freight.
  - ▶ This should improve their ability to avail and utilise input tax credits.
- ▶ For international shipping lines, the service recipient would be liable to pay service tax on reverse charge basis.
  - ▶ Service tax paid should be admissible as CENVAT credit to a manufacturers and service providers on fulfilment of prescribed conditions.

- ▶ Such services provided by a non-resident shipping company to a non-resident service recipient may not be taxable.
- ▶ Implications of these charges on freight forwarders need to be examined.
- ▶ Ocean freight forms part of assessable value for computation of customs duty under the Customs Act. The charge of service tax on ocean freight could lead to double taxation in certain cases.
- ▶ Services by way of transport of goods by an aircraft would continue to be tax free thereby resulting in a differential tax treatment for air freight.

#### Outbound Cargo

- ▶ Currently, services by way of transport of goods by vessel or aircraft for outbound shipment billed in India is not taxable as the place of provision is determined to be outside the taxable territory ie destination of goods. However, CENVAT credit is not available or triggers CENVAT credit reversal where such services do not qualify as export.
- ▶ The definition of exempted services has been amended to zero rate such services so that credit of input taxes would be available (wef 1 June 2016) to the service provider.
- ▶ Services by way of transportation of goods by an aircraft continue to be non-taxable and therefore, credit would be restricted if services do not qualify as export.

#### Coastal Transportation

- ▶ Currently, service tax is charged on 30 percent of freight without availing the CENVAT credit facility.

- ▶ The scheme has been amended to allow CENVAT credit of input services.

- ▶ Basic customs duty rate on import of refrigerated containers (8609 00 00) is reduced from 10 percent to 5 percent. Excise duty rate has been reduced from 12.5 percent to 6 percent.

#### B. Surface transportation

- ▶ Currently, no service tax is applicable on passenger transportation services (with or without accompanies belongings) by stage carrier.

- ▶ This is proposed to be amended to tax air conditioned contract carriage (wef 1 June 2016).

- ▶ Rationalisation of abatement rates and conditions in respect of following (wef 1 April 2016)

- ▶ Transport of goods and passengers by rail services, CENVAT credit of service tax paid on input services now available subject to conditions.

- ▶ Currently, an abatement of 60 percent is available in case of GTA services if no cenvat credit has been claimed by the GTA and service tax is charged on 30 percent of freight charges and thus the effective rate is 4.2 percent. The abatement in case of GTA services has been reduced from 70 percent to 60 percent for shifting of used household goods and making the effective service tax rate to 5.6 percent.

- ▶ For renting of motor vehicle the cost of fuel to be included in the value of taxable services for charging service tax.

#### C. Rail Transportation

- ▶ Haulage services provided by Indian Railways to Container Train Operators

(‘CTOs’) clarified to be transport of goods by rail.

- ▶ This will provide much needed relief to the industry as the issue of classification is in dispute for many industry players

- ▶ Demand notices have been issued classifying these services as support services by the Government and demanded service tax under reverse charge

- ▶ If services are classified to be support services by the Government, abatement would not have been available and service tax would have been charged at full rate.

- ▶ Transport of goods in containers (other than by Indian railways) is now entitled to 60 percent abatement and service tax to be charged on 40 percent. CENVAT credit paid on input services has been allowed.

- ▶ The definition of capital goods has been widened to include wagons of sub heading 8606 92 making it eligible item for claiming CENVAT credit.

- ▶ Basic customs duty rate on import of refrigerated containers (8609 00 00) is reduced from 10 percent to 5 percent. Excise duty rate has been reduced from 12.5 percent to 6 percent.

- ▶ Excise duty rate on goods falling under 8607 (parts of railway or tramway locomotives or rolling stock) and 8608 (railway or tramway track fixtures ad fitting etc) is reduced to 6 percent.

- ▶ Excise duty on some specified goods (capital goods, spare parts, raw material etc) for repair of ocean going vessels by a ship repair unit is exempted subject to actual user condition.

## CENVAT Credit

- ▶ Rationalisation of Rule 6 ie credit reversals in case of provision of exempted and non exempted services (wef 1 March 2016)
- ▶ Annual return is required to be filed by 30 November (wef 1 April 2016).
- ▶ Provisions with regard to utilisation of CENVAT credit on FIFO basis now omitted (wef 1 April 2016).
- ▶ Capital goods having value upto INR 10,000 per piece are included in the definition of inputs.

## CENVAT credit mechanism

- ▶ Cenvat credit has been entirely rationalised for service provider rendering both taxable and exempt services (wef April 2016).
- ▶ Need for maintaining separate records for inputs and input services removed.
- ▶ No reversal of credit required on input services exclusively used for provision of output services which are not exempted.
- ▶ Reversal of Cenvat credit to be computed only on common credits (ie credit of services used for providing both taxable and exempt services).
- ▶ Manner of determining whether Cenvat credit has wrongly utilised has been amended.
- ▶ Existing FIFO based method of determination removed. It needs to be evaluated whether taxpayer can maintain adequate Cenvat credit balance, thereby reducing interest exposure on disputed amounts where adequate balance exists.
- ▶ Cenvat credit on procurement of capital goods having value up to INR 10,000/- per piece shall be allowed in the first

year of purchase as they shall be considered as 'inputs'.

- ▶ Credit to be admissible in respect of equipment/ appliances in office located within a factory of manufacture to remove ambiguity.

## Other key proposals

- ▶ Facility of single-window clearance for customs to be implemented at major ports and airports in line with 'Less Government, More Governance' initiative.
- ▶ Provisions for deferred payment of customs duty have been introduced for importers and exporters with proven track records.
- ▶ Annual Return is to be filed by a manufacturer of final products or provider of output services for each financial year, by the 30th day of November of the succeeding year in the form as specified by a notification by the Board.
- ▶ Indirect Tax Dispute Resolution Scheme to be introduced with effect from 1 June 2016 for Customs, excise and service tax laws. Disputes pending before Commissioner (Appeals) for cases of tax / duty up to Rs 50 lacs to be eligible.
- ▶ 11 new benches of CESTAT to be established to reduce pendency
- ▶ No change in excise and customs duty rate
- ▶ The limitation period for recovery of service tax for cases involving non-evasion of service tax is enhanced from eighteen months to thirty months.

- ▶ No imprisonment in cases where the amount involved is equal to or less than INR 2 crore for the following punishable offences:
  - (i) Knowingly evades the payment of service tax;
  - (ii) Availing and utilizing credit of taxes without actual receipts of taxable services or excisable goods;
  - (iii) Maintaining false books of account or fails to supply any information or supplies false information;
- ▶ The power to arrest is restricted only to cases where an amount is collected as service tax but not paid.



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