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Alerts: BDO India: Countdown to the Budget 2023_Vol-1

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As the run-up to the India Union Budget 2023 begins,BDO India is pleased to share key expectations from this year's Budget announcements, in our Pre Budget campaign: Countdown to the India Union Budget 2023(a two-volume series)

The Year 2022 was marred with bouts of COVID-19 and geopolitical tensions. International markets have tumbled, and the global economy is staring at a recession. To tame these recessionary trends, the USA and several other countries have hiked their interest rates and are undertaking various measures. While India too hiked its interest rates, globally the country is seen as a silver lining amidst the dark clouds. With India in the spotlight and this being the last full budget before the general elections (scheduled next year), expectations are running high from all stakeholders. Some of the proposed policies that could be part of the upcoming Budget are outlined below:

- **Corporate Tax**
  - Rationalisation and simplification of the **capital gain tax regime**. Currently, there are multiple rates applicable depending on the nature of the taxpayer, the type of capital asset, the period of holding, etc. Similarly, for the financial asset class a single tax rate for long-term and short-term capital gains could be introduced, irrespective of the nature of investments, equity or debt, listed or not.
  - In respect of **unlisted shares** acquired before 31 January 2018 and sold under Offer for Sale during the Initial Public Offering with the levy of Securities Transaction Tax (before the listing date), there is no mechanism provided for computing the cost of acquisition. With a view to avoid litigation, suitable amendments may be made to provide a computation mechanism for such cases.
  - It is expected that the scope of section 45(5A) of the Income Tax Act, 1961 (IT Act), dealing with the taxation of joint development agreements may be extended to all taxpayers and include unregistered development agreements. Relaxations on stamp duty valuation may be extended to transactions covered by section 45(5A) of the IT Act.
  - Certain transactions like fresh issue of shares, buy back, right issue, Employee Stock Option Plan, Compulsorily Convertible Preference Shares / Compulsorily Convertible Debentures conversion may be excluded from taxability under the head 'Income from Other Sources'.
  - Currently, interest expense to the tune of 20% of dividend income is allowed as a deduction from the dividend income. Further, a deduction is prescribed where a company receiving a dividend has also declared dividend. In this regard, clarity may be given as to whether a deduction of 20% should be computed on the gross dividend or net dividend.

- **Transfer Pricing (TP)**
  - Exemption from filing Accountant's Report(Form 3CEB) for non-resident taxpayers who are exempted from filing Income Tax Returns.
  - Section 94B of the IT Act provides for a limitation on interest deduction where the borrowing is from a non-resident Associated Enterprise (AE). Further, the restriction also applies if the AE guarantees any loan taken by the company. In this regard, clarity may be brought in situations where the lender is an Indian resident, but the loan is guaranteed by a non-resident AE.

    - The Advance Pricing Agreement regime may be revamped by: (i) Prescribing maximum time-limit for completion; (ii) Relaxation of site visits / allowing online site visits; and (iii) Simple roll over of original APA for renewal etc.

- **Indirect Tax**
    - **Amendments pertaining to ITC**

      Presently, the GST law restricts ITC of GST suffered on premium paid for employee insurance unless such insurance is mandated by any law. It is expected that the law would be amended to allow ITC of GST suffered on employee insurance without restrictions, which is indeed an activity relating to the business of the taxpayer and medical cover is essential to attract and retain talent.

      Similarly, there are multiple restrictions on ITC, defeating one of the stated objectives of the introduction of GST, i.e., seamless flow of credits. It is expected that the Budget would revisit and relax the restrictions on ITC to pave way for seamless tax credit and removal of cascading of tax.

    - **Amendment in the Manufacturing and Other operation in Warehouse Regulation (MOOWR) scheme**

      The MOOWR scheme lacks clarity on at least two counts: (i) Duty exemption on the conversion of EOU units to MOOWR unit, and (ii) Grant of depreciation on capital goods removed from the units after use, to compute duty payable on such capital goods. It is expected that the Government will amend the provisions to clarify both.

- **Dispute resolution – Amnesty scheme**
    - An amnesty scheme that includes a waiver of penalties, on similar lines as the 'Vivaad se Vishwas' and 'Sabka Vishwas schemes', may be brought in to reduce the pendency of tax appeals before various forums. This would cover the Income Tax Act and Customs Act.
    - Another amnesty scheme to waive interest and penalties under the Customs Act, for failure to fulfil export obligations under export promotion schemes such as Advance Authorisation, EPCG, etc. is also expected. There is also an anticipation of an amnesty scheme to grant relief from interest and penalty levied for procedural lapses under GST laws during the initial years of its introduction.

- **Others**
    - **Solar Energy**

      The Indian Government is taking various initiatives to boost the usage of green energy. It is expected that the Budget may bring in tax benefits to the businesses generating green energy. This could be either in the form of a weighted deduction or a tax holiday.

    - **Start-ups**

      - Amendment to section 79 of the IT Act dealing with carry forward and set-off of losses to be extended to eligible start-ups even if only the original promoters continue to hold the shares in the year of set-off of losses.

      - Many start-ups incur huge initial set-up-related expenditures on which GST is levied and accumulated as Input Tax Credit (ITC). Currently, the law does not allow refund of accumulated ITC, resulting in working capital blockage for start-ups. An appropriate mechanism may be required to address such accumulation of ITC during the initial years of the set-up of the business to provide a facilitative ecosystem.

- **Insurance**
  - Currently, commission to an insurance agent is subject to a free look period. In case of a cancellation of a policy, the said commission is reversed. However, tax is withheld on gross commission without considering reversal due to policy cancellation. Hence, an amendment may be brought in to consider net commission.
  - As insurance companies have a long gestation period before they break-even, the period of 8 years for set-off and carry forward of business losses may be extended for insurance companies.
  - For computing book profits (for Minimum Alternate Tax purpose) of general insurance companies, clarity with respect to adjustment for Unexpired Risk Reserve may be provided.

Conclusion

Amidst global recessionary headwinds, India is expected to be an outlier demonstrating growth. All eyes will look towards the FM to display signs that India continues to remain a preferred destination for business growth. One important way that Budget 2023 could achieve this is by focusing on significant direct and indirect tax policy changes as an integral part of making India a preferred investment destination and thereby spurring economic growth. This budget will have to play a twin role of containing inflationary trends as well as bolstering opportunities to address the growth needs of the world's most populous country. It is expected that Budget 2023 could bring in the needed tax and fiscal policy reforms which will further its aim of becoming self-reliant and a serious global player.

We will be analysing the budget proposals as they are announced on **1 February 2023**.
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