INDIA'S BUDGET 2023-24 - KEY HIGHLIGHTS AND ANALYSES

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Introduction

India's Union Budget (the "**Budget**") was announced on February 1, 2023, and the Finance Bill, 2023 (the "**Finance Bill**") was tabled in Parliament. The Finance Bill will be discussed in Parliament before its enactment, and therefore, it is likely that the Finance Bill may be amended because of these discussions. Once enacted, unless specified otherwise, most of the income tax proposals in the Finance Bill will be effective from the financial year commencing on April 1, 2023.

We have summarized below some of the key income tax proposals made in the Budget. Note that 1 lac is 100,000 and 1 crore is 10,000,000.

Personal income tax rates

The Finance Bill has introduced a new personal income tax regime. Under the Income-tax Act, 1961 (the "**IT Act**"), the below listed tax rates will be available to an individual taxpayer if he/she agrees to let go of all tax deductions or exemptions (mentioned below).

Sl. No	Total income	Rate of tax
1.	Up to INR 300,000	Nil
2.	INR 300,001 to INR 600,000	5%
3.	INR 600,001 to INR 900,000	10%
4.	INR 900,001 to INR 1,200,000	15%
5.	INR 1,200,001 to INR 1,500,000	20%
6.	Above INR 1,500,000	30%

In addition, the surcharge on income tax has also been reduced as below.

Sl. No	Taxable Income	Surcharge rate
1.	Above INR 50 lacs but up to INR 1 crore (including dividend income and capital gains)	10%
2.	Above INR 1 crore up to INR 2 crore (including dividend income and capital gains)	15%
3.	Above INR 2 crore up to INR 5 crore (excluding dividend income and capital gains)	25%
Additionally, a 4% Health and Education Cess will also be attracted.		

The key conditions that will have to be satisfied are:

a) No exemptions or deductions are claimed for leave travel concession, house rent allowance, standard deduction, or interest on housing loan for self-occupied property or

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vacant property;

b) No deductions are claimed in respect of payments towards insurance, provident funds, mediclaim premiums, donations (except for contribution to National Pension Scheme or the deduction under Section 80JJAA of the IT Act for recruiting new employees);

c) Brought forward losses or unabsorbed depreciation pertaining to the above deductions are not set off in future years;

d) Loss under the head of "house property" is not set off against any other head of income; and

e) No exemption or deduction is claimed for any other allowance or perquisite.

If an individual (who is less than 60 years of age) seeks to avail the foregoing tax deductions, then such individual will have the option to choose the following slab rates.

Sl. No	Total income	Rate of tax
1.	Up to INR 300,000	Nil
2.	INR 300,001 to INR 500,000	5%
3.	INR 500,001 to INR 1,000,000	20%
4.	INR 1,000,001 and above	30%

Surcharge and health and education cess will apply as mentioned in the table above.

The revised personal income tax rate changes appear attractive and may benefit several salaried taxpayers; however, we recommend that a tax comparative analysis is carried out to check if the tax benefits are different if the individual salaried taxpayer avails the tax deductions and exemptions. Separately, reduction in the surcharge from 37% to 25% for high income earners is an unexpected but welcome change.

This amendment will take effect from April 1, 2023.

No tax up to INR 7 lacs for Indian individual residents

Under the current provisions of Section 87A of the IT Act, an Indian individual resident having a total income of less than INR 5 lacs is permitted a rebate of 100% of the amount of income tax payable, effectively paying no tax.

With effect from April 1, 2023, the Finance Bill has proposed that an individual resident in India whose income is chargeable to tax will now be entitled to a 100% rebate of the income tax payable on a total income not exceeding INR 7 lacs.

This will benefit the Indian middle-class taxpayer.

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Tax Incentives for units located in the International Financial Services Centre

Over the past few years, tax concessions have been provided to units located in the International Financial Services Centre ("**IFSC**"). In order to further incentivize operations from the IFSC, the Finance Bill has proposed to provide the following additional benefits:

a) an extension of the date for transfer of assets of the original fund, or of its wholly owned special purpose vehicle, to a resultant fund in case of relocation from the current date of March 31, 2023 to March 31, 2025.

b) a tax exemption on incomes distributed on offshore derivative instruments that fulfil certain conditions (to be prescribed in due course) so as to avoid double taxation.

This amendment will take effect from April 1, 2023.

Extending the tax exemption to foreign funds relocating to the IFSC until March 31, 2025 is a welcome move that is aligned with the Indian government's initiative to encourage financial institutions and fund managers to set up in the IFSC and compete in the international market through a globally competitive platform offering varied financial products and services.

Ease in claiming amortization of preliminary expenditure

Currently, Section 35D of the IT Act allows for amortization of certain preliminary expenses incurred prior to the commencement of business or after commencement in connection with extending the business undertaking or setting up of a new unit. This includes expenditure in connection with preparation of a feasibility report, project report, etc., but only if carried out either by the assessee or by a firm approved by the Central Board of Direct Taxes (the "**Board**").

The Finance Bill proposes to remove the condition that preparation of the report should be by a firm approved by the Board. Instead, the assessee will be required to furnish a statement containing the particulars of the expenditure, within a prescribed period to the prescribed income tax authority in the prescribed form and manner (expected to be provided in due course).

This amendment will take effect from April 1, 2023.

The Finance Bill's initiative in this regard represents an effort to create a more business-friendly environment and helps in ease of doing business.

Increase in threshold limits for presumptive taxation

The current provisions of Section 44AD of the IT Act, *inter alia*, provide for a presumptive income scheme for small businesses. This scheme applies to certain resident taxpayers (i.e.,

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an individual, Hindu Undivided Family or a partnership firm) carrying on an eligible business and having a turnover or gross receipt of INR 2 crores or less. Under this scheme, a sum equal to 8% or 6% of the turnover or gross receipts is deemed to be the profits and gains from business, subject to certain conditions. The Finance Bill has increased the threshold limit to INR 3 crores where the amount or aggregate of the amounts received during the previous year, in cash, does not exceed 5% of the gross receipts.

Section 44ADA of the Act provides for a presumptive income scheme for small professionals who are engaged in a prescribed profession and whose total gross receipts do not exceed INR 50 lacs in a financial year. Under this scheme, a sum equal to 50% of the gross receipts is deemed to be the profits and gains from business. The Finance Bill has increased the threshold limit to INR 75 lacs where the amount or aggregate of the amounts received during the previous year, in cash, does not exceed 5% of the total turnover or gross receipts.

These amendments will take effect from April 1, 2023.

This is line with various representations that were made to the government for increasing the thresholds for eligibility to avail the benefit of the presumptive schemes for eligible business and professions in order to do away with mandatory statutory audits, expand the tax base and benefit more small and medium businesses.

Tax deduction at source and taxability on net winnings from online games

Section 194B of the IT Act provides that the person responsible for paying to any person any income by way of winnings from any lottery or crossword puzzle or card game and other game of any sort in an amount exceeding INR 10,000 shall deduct income tax at the rates in force.

Section 194BB of the IT Act makes similar provisions for deduction of tax at source for horse racing in any racecourse or for arranging of wagering or betting in any racecourse.

Section 115BB of the IT Act provides for the rate of tax on winnings from lotteries, crossword puzzles, races (including horse races), card games and other games of any sort or gambling or betting of any form or nature.

It was seen that deductors are deducting tax under Section 194B and 194BB of the IT Act by applying the threshold of INR 10,000 per transaction and avoiding the aforesaid tax deduction by splitting a winning into multiple transactions each below INR 10,000, which was not the legislative intent. Moreover, in recent times, there has been a rise in the users of online games, and therefore, a need was felt to bring in specific provisions regarding withholding taxes and taxability of online games due to their different nature (being easily accessible via the internet and computer resources with a variety of playing options and payment options).

Accordingly, the Finance Bill has proposed to:

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a) to amend Sections 194B and 194BB of the IT Act to provide that deduction of tax under these sections shall be on the amount or aggregate of amounts exceeding INR 10,000 during the financial year;

b) to amend Section 194B of the IT Act to include "gambling or betting of any form or nature whatsoever" within its scope;

c) to amend Section 194B of the IT Act to exclude online games from the purview of this section from July 1, 2023, as a new Section 194BA has been proposed to be introduced for deduction of tax at source on winnings from online games from that date;

d) to insert a new Section 194BA in the IT Act, with effect from July 1, 2023, to provide for deduction of tax at source on net winnings in the user account at the end of the financial year; and

e) to provide definitions of "computer resource," "internet," "online game," "online gaming intermediary," "user," and "user account" in the proposed Section 194BA;

The amendments proposed for Section 194B and Section 194BB of the IT Act will take effect from April 1, 2023. The proposed Section 194BA of the IT Act will come into effect from July 1, 2023. The amendment proposed for Section 115BB of the IT Act will take effect from April 1, 2024.

The Finance Bill has introduced this provision to improve tax compliance and administration, widen the tax base to cover online games and to check tax withholding leakages.

Special provision for taxation of capital gains in case of Market Linked Debentures

It was noticed that a variety of hybrid securities that combine features of plain vanilla debt securities and exchange traded derivatives were being issued through private placements and listed on stock exchanges. Such securities, i.e., Market Linked Debentures, were taxed as long-term capital gains at the rate of 10% without indexation, instead of as short-term capital gains, although they were in the nature of derivatives.

Therefore, it has been proposed to insert a new Section 50AA in the IT Act to treat the full value of the consideration received or accruing as a result of the transfer, redemption or maturity of Market Linked Debentures (as reduced by the cost of acquisition of such debentures and the expenditure incurred wholly or exclusively in connection with transfer or redemption of such debentures) as capital gains arising from the transfer of a short-term capital asset.

Further, it is also proposed to define the "Market Linked Debenture" as a security by whatever name called, which has an underlying principle component in the form of a debt security and where the returns are linked to market returns on other underlying securities or indices and includes any securities classified or regulated as a Market Linked Debenture

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by the Securities and Exchange Board of India.

While some may say that this change was overdue, bringing short-term capital gains taxation regime for Market Linked Debentures may impact the overall attractiveness of the instrument for investors.

This amendment will take effect from April 1, 2023.

Reduction for time provided to furnish transfer pricing report

The Finance Bill proposes to amend Section 92D(3) of the IT Act to provide that the Assessing Officer or the Commissioner (Appeals) may, in the course of any proceeding under the IT Act, require any person who has entered into an international transaction or a specified domestic transaction to furnish information or document within a period of 10 days (currently 30 days) from the date of receipt of a notice issued in this regard, which may be extended by a further period not exceeding 30 days.

This amendment will take effect from April 1, 2023.

Shares issued to non-residents at a premium

Section 56(2)(viib) of the IT Act, *inter alia*, provides that where a company (not being a company in which the public are substantially interested) receives, in any previous year, from any person being a resident, any consideration for issue of shares that exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds the fair market value of the shares shall be chargeable to income tax under the head income from other sources.

Rule 11UA of the Income-tax Rules provides the formula for computation of the fair market value of unquoted equity shares for the purposes of the Section 56(2)(viib) of the IT Act. The provision was introduced by the Finance Act, 2012 to prevent generation and circulation of unaccounted money through share premium received from resident investors in a closely held company in excess of its fair market value. However, this section was not applicable for consideration (share application money or share premium) received from non-resident investors.

The Finance Bill has proposed to include the consideration received from a non-resident also under the ambit of Section 56(2)(viib) of the IT Act. This will make the provision applicable to receipt of consideration for issue of shares from any person irrespective of his residency status.

The amendment will be effective from April 1, 2023.

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The Finance Bill has introduced this provision to all persons (residents or non-residents) as a tax anti-avoidance measure. However, it brings back fears of tax overreach for non-resident investors investing in Indian start-ups.

Time limits for bringing consideration against export proceeds into India

The current provisions of the Section 10AA of the IT Act, *inter alia*, provide a 15-year tax holiday to a unit established in a special economic zone ("**SEZ**") that has begun operations before September 30, 2020. However, no time limit has been prescribed in the IT Act for remitting export proceeds to the SEZ units from the sale of goods or provision of services by them.

The Finance Bill has proposed to provide that the deduction under Section 10AA of the IT Act shall only be available for such SEZ units if the proceeds from sale of goods or provision of services is received in, or brought into, India by the assessee in convertible foreign exchange within a period of 6 months from the end of the previous year or within such further period as the competent authority may allow. The competent authority shall mean the Reserve Bank of India or such authority as is authorized under any law for the time being in force for regulating payments and dealings in foreign exchange. The Finance Bill clarifies that the export proceeds from sale of goods or provision of services shall be deemed to have been received in India when such proceeds are credited to a separate account maintained for the purpose by the assessee with any bank outside India with the approval of the Reserve Bank of India.

The amendment will be effective from April 1, 2023.

The Finance Bill has introduced this provision to hold SEZ units responsible for bringing into India payments from sale of goods or services within a stipulated time and not leaving foreign exchange outside India. SEZ units will now have to update their foreign customers on this new rule, so that invoice payment cycles can be reworked accordingly.

Promoting timely payments to Micro and Small Enterprises

In order to promote timely payments to micro and small enterprises ("**MSME**"), the Finance Bill has proposed to insert a new clause (h) in Section 43B of the IT Act to provide that any sum payable by a taxpayer to the MSME beyond the time limit specified in Section 15 of the MSME Development Act, 2006 shall be allowed as a deduction only on actual payment. Section 15 of the MSME Development Act, 2006 mandates payments to MSMEs within the time prescribed as per the written agreement, which is capped at 45 days, and if there is no such written agreement, the payment is required to be made within 15 days.

This amendment will take effect from April 1, 2023.

The Finance Bill has brought in this provision to enable MSMEs to receive timely payments failing which the payer will not be allowed a business deduction, which is welcome move for

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MSMEs.

Relief to start-ups in carrying forward and setting off of losses

Section 79 of the IT Act *inter alia* prohibits setting off carried forward losses if there is a change in the shareholding of the company. Section 80-IAC of the IT Act exempts eligible start-ups from this provision subject to certain conditions. One condition is that the loss should have been incurred during a period of 7 years from the date of incorporation. The Finance Bill has proposed to provide the benefit of carry forward of losses on a change of shareholding for start-ups for a period of 10 years from the date of incorporation.

The above amendment will take effect from April 1, 2023.

This provision will encourage and help start-ups that may have incurred substantial business losses during the pandemic period.

Extension of date of incorporation for eligible start-ups for exemption

Under the provisions of the section 80-IAC of the IT Act, a deduction of 100% of the profits and gains derived from an eligible business by an eligible start-up for 3 consecutive assessment years out of 10, beginning from the year of incorporation, at the option of the taxpayer, is allowed subject to certain conditions. One condition is that the eligible start-up should be incorporated on or after April 1, 2016 but before April 1, 2023. In order to further promote the development of start-ups in India, the Finance Bill has proposed to extend the period of incorporation of eligible start-ups to April 1, 2024.

The amendment will be effective from the April 1, 2023.

In the last year's budget, the Indian government had extended the date of incorporation for this tax exemption until March 31, 2023, citing delay in setting up of start-ups due to Covid-19. Extending the date of incorporation by one more year is one of the steps the Indian government is taking to encourage the start-up ecosystem, alongside initiatives like the Start-up India initiative, the Fund of Funds for Start-ups (FFS) scheme, the Start-up India Seed Fund Scheme (SISFS) and the Credit Guarantee Scheme for Start-ups (CGSS).

Conversion of gold to electronic gold receipts

The Finance Bill has proposed to exclude the conversion of physical form of gold into Electronic Gold Receipts ("**EGR**") and *vice versa* by a Securities and Exchange Board of India ("**SEBI**") registered Vault Manager from the purview of "transfer" for the purposes of capital gains tax. Further, the Finance Bill has proposed that the cost of acquisition of the EGR for computing capital gains shall be deemed to be the cost of gold in the hands of the person in whose name the EGR is issued, and the holding period for the purpose of capital gains will include the period for which the gold was held by the assessee prior to its conversion into EGR.

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The amendment will take effect from April 1, 2024.

EGRs are depository gold receipts traded on the stock exchanges. Under this form, investors can buy the gold in dematerialised form and are given gold receipts instead of physical gold. As the conversion of physical gold into EGR and vice versa is proposed not to be treated as a transfer, such conversion will not attract any capital gains tax. This is very good move.

Facilitating certain strategic disinvestments

To facilitate certain strategic disinvestments, the Finance Bill has proposed to allow carry forward of accumulated losses and unabsorbed depreciation allowance in the case of amalgamation of one or more banking company with any other banking institution or company subsequent to a strategic disinvestment, if such amalgamation takes place within 5 years of the strategic disinvestment.

In the IT Act, "strategic disinvestment" has been defined as sale of shareholding by the Central Government or any State Government in a public sector company which results in reduction of its shareholding below 51% along with transfer of control to the buyer.

The Finance Bill has proposed to modify the definition of "strategic disinvestment" to mean sale of shareholding by the Central Government, the State Government or Public Sector Company in a public sector undertaking or company which results in (i) reduction of its shareholding below 51%, and (ii) transfer of control to the buyer.

The amendment will be effective from April 1, 2023.

As the Indian government along with the Life Insurance Corporation of India prepare to divest their stake in IDBI Bank, the current provisions of the IT Act could have been a hindrance to the potential buyer to carry forward IDBI Bank's accumulated tax losses. Allowing carry forward of accumulated losses and unabsorbed depreciation in amalgamations will provide a good impetus for private banks to amalgamate with IDBI Bank and boost the government's revenue targets from disinvestments.

Extending the scope for deduction of tax at source to lower or nil rate

Section 197 of the IT Act provides for a grant of a certificate of tax deduction at lower or nil rate if the tax is required to be deducted under certain specified sections of the IT Act. The specified sections do not include Section 194LBA which provides that a business trust shall deduct and deposit tax at the rate of 5% on interest income of non-resident unit holders.

The Finance Bill has proposed to amend section 197(1) of the IT Act to provide that the sums on which tax is required to be deducted under section 194LBA of the Act shall also be eligible for certificate of deduction at a lower rate.

This amendment will take effect from April 1, 2023.

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Extending deeming provisions of gift taxation to not-ordinarily resident persons

The Finance Act, 2019 introduced the provision that a sum of money exceeding INR 50,000, received by a non-resident without consideration from a person resident in India, on or after the July 5, 2019, shall be considered as income deemed to accrue or arise in India, and will be taxable accordingly. It came to notice that certain persons being not-ordinarily resident were receiving gifts from persons resident in India and not paying tax. The Finance Bill has proposed to extend this deeming provision to a sum of money exceeding INR 50,000 received by a not-ordinarily resident person, without consideration, from a person resident in India.

This amendment will be effective from April 1, 2024.

This proposal is an anti-abuse provision to prevent not-ordinarily resident persons from not paying tax on the gifts received from persons resident in India.

Removal of exemption from tax withholding on interest payments on listed debentures to a resident

The IT Act provides for a tax withholding on payment of interest income (on securities) to a resident; however, a recipient is exempted from a tax withholding where the security is in dematerialized form and is listed on a recognized stock exchange in India in accordance with the Securities Contracts (Regulation) Act, 1956 and the rules made thereunder. Considering the under reporting of interest income by the recipients due to the above tax withholding exemption, the Finance Bill has proposed to withdraw the exemption.

The amendment will be effective from April 1, 2023.

The Finance Bill has introduced this provision as an anti-abuse provision to block tax leakages.

Preventing misuse of presumptive schemes under section 44BB and section 44BBB

Section 44BB and Section 44BBB of the IT Act, applicable on a non-resident assessee and a foreign company, respectively, provide for a presumptive tax scheme, where a sum equal to 10% of the aggregate of the amount paid or payable is deemed to be the profits and gains chargeable to tax. The taxpayers often opt for presumptive taxation in profitable years and opt out of presumptive taxation when losses occur.

To avoid such misuse, for non-residents, the Finance Bill has proposed that where a non-resident assessee declares profits and gains of business for any previous year in accordance with the provisions of presumptive taxation, unabsorbed depreciation and brought forward loss shall not be allowed to be set off.

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The amendment will take effect from April 1, 2023.

Through this amendment, the Finance Bill is seeking to prevent the misuse of the presumptive schemes by non-residents.

Increasing rate of Tax Collection at Source (TCS) of certain remittances

The Finance Bill has proposed to increase the rate of TCS for foreign remittances for "other purposes" (except for education purposes and medical treatment) under the Liberalized Remittance Scheme and purchase of overseas tour package from 5% to 20%.

This amendment will be effective from July 1, 2023.

Restrictions on claiming benefit under section 54 and 54F of the IT Act

Section 54 and 54F of the IT Act provides for an exemption from capital gains in respect of acquisition of a residential house property. The Finance Bill has now proposed that for working out the exemption under these sections, the investment in residential property above INR 10 crore shall be ignored.

The amendment will be effective from April 1, 2023.

The Finance Bill explains that the primary objective of Section 54 and of the IT Act was to mitigate the acute shortage of housing and to give impetus to house building activity. However, it has been observed that claims of huge deductions by high-net-worth taxpayers are being made under these provisions when purchasing expensive residential houses, which defeats the very purpose of these sections.

Cost of acquisition and improvement for self-generated intangible assets and rights

The Finance Bill has proposed that the cost of improvement of any intangible asset or any other right shall be nil. Similarly, the cost of acquisition of any intangible asset or any other right shall be nil, except where it is acquired for a consideration.

The amendment will be effective from April 1, 2023.

The existing provisions of the Section 55 of the IT Act, *inter alia*, define the "cost of any improvement" and "cost of acquisition" for the purposes of computing capital gains. However, for certain assets, like intangible assets or rights, no consideration is paid for acquisition. The cost of acquisition of such assets is not clearly defined as "nil" in the present provision, which has led to legal disputes in which courts have held that for taxability under capital gains there has to be a definite cost of acquisition, else it will be deemed as nil under the IT Act. The Finance Bill proposes to introduce a provision to this effect.

Prevention of double deduction claimed on interest paid for property

In cases where interest on borrowed capital for acquisition of house property has been allowed as a deduction while computing income from house property or under any other provision of the IT Act, then such interest shall not be included in the cost of acquisition or cost of improvement of the house property transferred.

The amendment will be effective from April 1, 2023.

It is to be noted that taxpayers used to first claim a deduction on the interest on borrowed capital for acquiring a house under Section 24 of the IT Act under the head "income from house property" and then, also compute the same amount as a cost of acquisition to reduce their "capital gains" under section 48 of the IT Act. The Chennai Tribunal in the *C. Ramabrahmam* case held that a double deduction is only possible when none of the two provisions exclude the operation of the other. The Finance Bill seeks to plug the loophole.

Taxability of distributions other than dividend/ interest/ rental income

The Finance Bill has proposed that amounts received by unitholders from REITs/InvITs in the nature of repayment of debt by the SPVs are proposed to be taxed as income from other sources. Further, in case of a distribution on account of redemption of units, amounts received in excess of the cost of acquisition shall be taxable as income from other sources.

The amendment will be effective from April 1, 2023.

The Finance Bill suggests that incomes in the nature of interest, dividend and rental income have been accorded a pass-through status at the level of a business trust and are taxable in the hands of the unit holder. However, in respect of the distributions made by the business trust to its unit holders which are shown as repayment of debt, it is actually an income of the unit holder that does not suffer taxation either in the hands of business trust or in the hands of unit holder, which is not the legislative intent. Accordingly, the Finance Bill has proposed to make repayment of debt received by a unit holder taxable. This will have a major impact on non-resident sponsors as such distributions will be taxed at approx. 43.68%. The point that is likely to be debated is how can repayment of a debt or loan be characterized as income in the first place.

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