

Key amendments to Finance Bill, 2023

28 March 2023



Summary

The Finance Bill, 2023, (the Finance Bill) was introduced in the Lok Sabha by the Finance Minister on 1 February 2023. Based on inputs and representations received from various stakeholders, certain amendments (FBA 2023) have been proposed to the Finance Bill. These amendments have been approved by the Lok Sabha and Rajya Sabha. However, the Finance Bill is yet to receive the President's assent.

The key amendments are:

Direct tax

Key amendments relating to the financial services sector

Non-applicability of surcharge and cess on certain incomes earned by specified funds in the International Financial Service Centre (IFSC)

- As per the FBA 2023, surcharge and cess would not be applicable while computing advance tax on the prescribed income¹ earned by the specified funds².

Taxability of dividend income received by non-resident from a unit in IFSC

- The FBA 2023 mandates that dividend received by a non-resident (NR) / foreign company from a unit in the IFSC will be taxable at 10%³ (plus applicable surcharge and cess).

Expansion of definition of original fund in case of relocation to IFSC

- The FBA 2023 has extended the definition of 'Original Fund'⁴ to include an investment vehicle in which the Abu Dhabi Investment Authority (ADIA) is the direct or indirect sole shareholder or unitholder or beneficiary or interest holder and it is wholly owned and controlled directly or indirectly by the ADIA or the Government of Abu Dhabi.
- Additionally, the original fund would also include any fund, as may be notified by central government.

Relaxation of condition prescribed for tax exemption of Offshore Derivative Instruments (ODI)

- The Finance Bill proposed to exempt the income of NR as a result of distribution of income on ODIs⁵, to the extent such income is chargeable to tax in the hands of the offshore banking unit in the IFSC (IBU) registered as 'Foreign Portfolio Investor'.

1 Income covered by Section 115AD(1)(a) of the Act
2 As defined in clause (c) of Explanation to section 10(4D) of the Act
3 Section 115A of the Act

4 As defined in explanation to Section 47(viiac) and 47(viiad) of the Act
5 Section 10(4E) of the Act

- As per the FBA 2023, the condition of such income being chargeable to tax in the hands of the IBU has been removed.

Concessional tax rate on interest income on specified bonds listed on stock exchange in IFSC

- Currently, the interest income received by NR/foreign company from specified bonds⁶ issued before 1 July 2023 and which are listed on stock exchanges in the IFSC is taxed at 4%.
- As per the FBA 2023, interest income received by NR/foreign company on specified bonds⁶ issued on or after 1 July 2023 and listed on stock exchanges in the IFSC will be taxable at 9%.

Exemption on certain income of NR received in IFSC

- Currently, exemption is provided to NR on income earned from the portfolio of securities managed by a portfolio manager in the IFSC, which was accruing or arising outside India and is not deemed to accrue or arise in India and was received in an account maintained with the IBU⁷.
- As per the FBA 2023, this exemption would be provided, if prescribed activities are carried out by specified persons, as may be notified by the central government.

Tax holiday extension to Offshore Banking Unit (OBU) in Special Economic Zone (SEZ)

- Currently, tax deduction is provided to OBU in SEZ⁸ on their income to the extent of:
 - 100% of the income for 5 consecutive years from the year in which permission⁹ for the setup of OBU was obtained; and
 - 50% of the income for the next 5 years.
- As per the FBA 2023, instead of 50%, deduction for 100% of profits would be provided to OBUs (i.e. for year 6 to 10) for AY¹⁰ commencing on or after 1 April 2023.

Exemption provided to aircraft leasing entities in IFSC

- As per the FBA 2023, the sale of equity shares of a domestic company being a IFSC unit engaged primarily in aircraft leasing to a NR or another IFSC unit engaged primarily in aircraft leasing would be exempt¹¹ if:
 - Operations of such company have commenced on or before 31 March 2026; and
 - Capital gains should have arisen within a period of 10 years from the year in which such company has commenced operations or AY 2034-35, whichever is later.

6 Long-term bond or rupee denominated bond

7 As per Section 10(4G) of the Act

8 As per 80LA of the Act

9 Under Section 23(1)(a) of the Banking Regulation Act, 1949 or permission / registration under the SEBI Act, 1992 or any other relevant law

10 Assessment Year

11 Section 10(4H) of the Act

- Further, dividend income received by a unit in the IFSC engaged primarily in aircraft leasing from another unit in the IFSC also engaged primarily in aircraft leasing would be exempt¹².

Ship leasing entities in IFSC can opt for tonnage tax scheme

- The FBA 2023 stipulates that ship leasing entities in the IFSC can opt for tonnage tax scheme¹³ within a period of three months from the end of their tax holiday period¹⁴.

Taxation of sum received from business trust

- The Finance Bill had introduced provisions¹⁵ to tax 'specified sum' received by a unit holder from a business trust.
- The FBA 2023 has now prescribed the formula of computing the specified sum.

Capital gains

Units of business trust

- The FBA 2023 has provided that the cost of acquisition of a unit of a business trust shall be reduced by (and shall be deemed to always have been reduced by) any sum received by a unit holder from a business trust, except the income received under certain specified sections.

Market-linked debentures and specified mutual funds

- The Finance Bill had proposed to introduce a special provision¹⁶ for taxing capital gains on transfer / redemption / maturity of market-linked debenture¹⁷.
 - Such gains would be deemed to be short-term capital gains.
 - Cost of acquisition and expenditure incurred for transfer / redemption / maturity would be allowed (except STT¹⁸ paid).
- The FBA 2023 has expanded the scope of these provisions¹⁶ and such provisions would now apply to 'units of specified mutual funds' as well, if such units are acquired on or after 1 April 2023.
- Specified mutual fund means a mutual fund where not more than 35% of its total proceeds is invested in the equity shares of domestic companies¹⁹.

New tax regime (default regime)

- The Finance Bill 2023 had proposed to provide a rebate²⁰ under the new tax regime²¹ for taxpayers having taxable income up to INR 7 lakhs.
 - Amount of rebate: tax on total income or INR 25,000, whichever is lower.
- In order to make this regime more lucrative, the FBA 2023 has introduced a marginal relief provision for taxpayers in

12 Section 10(34B) of the Act

13 Section 115VP of the Act

14 As per section 80LA of the Act

15 Section 56(2)(xii) of the Act

16 Section 50AA of the Act

17 Market-linked debenture means a security by whatever name called, which has an underlying principal component in the form of a debt security and where the returns are linked to the market

returns on other underlying securities or indices, and includes any security Classified or regulated as a market-linked debenture by the Securities and Exchange Board of India.

18 Securities Transaction Tax

19 Shareholding should be computed with reference to the annual average of the daily closing figures

20 Section 87A of the Act

21 Section 115BAC of the Act

cases where tax on income exceeding INR 7 lakhs is more than the marginal income (i.e. the amount of tax > amount of income exceeding INR 7 lakhs).

Online gaming

Withholding tax on income from online gaming

- The Finance Bill introduced a special provision for withholding tax on income from online gaming²², which was proposed to be effective from 1 July 2023.
- These provisions would now be effective from 1 April 2023.

Higher withholding tax rate for non-filers

- Currently, deductors are required to withhold tax²³ at a higher rate²⁴ for certain specified payments to taxpayers who have not filed return of income.
- As per the FBA 2023, this provision would not apply in case of withholding tax on income from online gaming.

Tax collection at source (TCS)

Liberalised remittance scheme (LRS)

- Under the existing provisions, tax is required to be collected by the authorised dealer on remitting funds outside India under the LRS²⁵. The term 'outside India' has been deleted from these provisions as per the FBA 2023.

Higher TCS in certain cases

- Currently, TCS is required to be collected at a higher rate in the following cases:
 - The payer fails to furnish PAN²⁶;
 - The payer has not filed income tax return for the Financial year (FY)²⁷ immediately preceding the FY in which tax is required to be collected²⁸.
- As per the FBA 2023, the higher rate of TCS has been capped at 20% in such cases.

Taxation of non-residents / foreign company

- As per the FBA 2023, withholding tax rate for payment of royalty and fees for technical services (FTS)²⁹ to a NR / foreign company has been increased to 20%³⁰ (which was earlier 10%).

Indirect tax

Changes in GST law

Persons not liable for registration

- The Finance Bill proposed that where the person is engaged exclusively in making exempt supplies or has been specifically exempted from obtaining registration through a notification, the

22 Section 194BA of the Act

23 Section 206AB of the Act

24 Higher of the following:

a) Twice the rate specified in the relevant provision of the Act;

b) Twice the rate or rates in force;

c) At the rate of 5%.

25 Section 206C(1G) of the Act

26 Section 206CC of the Act

27 If such return of income is not filed within the time limit prescribed in Section 139(1) of the Act and the aggregate amount of tax deducted at source and TCS is INR 50,000 or more in the said FY

28 Section 206CCA of the Act

29 Section 115A of the Act

30 Plus applicable surcharge and cess

provisions of compulsory registration will not apply.

- However, the FBA 2023 has replaced Section 23(2) of the CGST Act³¹, not the entire Section 23. Accordingly, compulsory registration will not be required only in cases where the person is specifically exempted by the government to take registration³².

Revocation of cancellation of registration

- At present, the time limit for filing an application for the revocation of cancellation of registration is 30 days from the date of service of the cancellation order. The FBA 2023 has removed the time limit of 30 days. The time and manner of filing such an application shall be prescribed.
- The FBA 2023 has omitted the proviso empowering the authorities to extend the time limit.

Assessment of non-filers of returns

- In FBA 2023, the time limit to furnish a valid return by the registered person is extended from 30 days of the service of the assessment order to 60 days of the service of the assessment order in cases where the proper officer has assessed the tax liability on a best judgement assessment basis.
- In addition, a further 60-day extension is provided, subject to a late fee of INR 100 for each day of delay beyond 60 days of service of the said assessment

order, if the registered person fails to file a return within such time limit.

Constitution of Appellate Tribunal and benches thereof and related amendments

- In the FBA 2023, the jurisdiction, powers and authority conferred on the Appellate Tribunal to be exercised by the Principal Bench and State Benches instead of the National Bench or State Bench of the GST Appellate Tribunal (GSTAT).
- Accordingly, the entire provisions pertaining to the constitution of the Appellate Tribunal, qualification, appointment, conditions of service of the President and members of the Appellate Tribunal, and the financial and administrative powers of the President over the Appellate Tribunal are substituted.

Place of supply of services of transportation of goods

- In case where the supplier or recipient is located outside India, the specific provision to determine the place of supply of goods transportation services is omitted by the FBA 2023. Accordingly, the place of supply shall be determined as per the general provisions, i.e., the location of the recipient of services.

Schedule to the Goods and Services Tax (Compensation to States) Act, 2017

- In FBA 2023, schedule pertaining to the maximum rate at which the compensation cess may be collected for items such as *pan masala*, tobacco, and manufactured tobacco substitutes,

³¹ Central Goods and Service Tax Act, 2017

³² Issued under Section 23(2) of Central Goods and Services Tax Act, 2017

including tobacco products has been amended.

Changes in Customs law

New Section 65A inserted to provide for payment of certain taxes on goods to be deposited in warehouse for operations

- Currently, all customs duties on goods imported in a customs bonded warehouse under the Manufacture and Other Operations in Warehouse Regulations (MOOWR) are deferred. Such duties are payable on clearance of goods from the warehouse for home consumption.
- In the FBA 2023, the deferment is to be restricted to duties other than integrated tax (IGST) and compensation cess (Cess). In other words, IGST and Cess

are payable on the import of goods under MOOWR.

- The amendment will not apply in respect of goods deposited or permitted to be removed for deposit in the warehouse before the effective date of the provision.
- The government also has power to notify certain goods on which the new provisions will not apply.

Other related amendments

- In the FBA 2023, amendments have been made in Section 157 (General powers to make regulation) and Section 159 (Rules, certain notifications, and orders to be laid before the parliament) to empower the Board to make regulations regarding the manner and conditions of payment of duty and the removal of goods u/s 65A.

Our comments

As a welcome move, several benefits have been provided for further promoting the IFSC, which is likely to provide fillip to the financial services ecosystem in India.

Increase in withholding tax rate for royalty and FTS payments to non-residents / foreign companies to 20% (plus applicable surcharge and cess) will impact entities that are located in jurisdictions which do not have a tax treaty with India or where the treaty benefit is not available due to any other reason. Further, Indian entities who are contractually bearing taxes in such cases may need to evaluate if re-negotiation of contracts is required.

On the indirect taxes front, the constitution of the GST Appellate Tribunal has been pending since the inception of the GST regime. In this regard, the amendments proposed in the FBA 2023 would provide a huge relief to the taxpayers, streamline the litigation process, and reduce unnecessary burden on the high courts.

Furthermore, the amendments related to the payment of IGST and compensation cess in case of deposit of goods in a custom-bonded warehouse for manufacturing and other operations is quite unexpected. In this scenario, the restriction on deferment of IGST and compensation cess (unlike other duties) will have a significant impact on the working capital of the importers.

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