Tax Alert: Finance Act 2020 gets enacted

Issued on 1 April 2020

Summary

The Finance Bill, 2020, received President's assent on 27 March 2020. The Finance Act, 2020, ('the Finance Act') has amended various provisions proposed in the Finance Bill including:

- In order to determine the residential status and also for the purpose of citizenship-based deemed residency, introducing a de-minimis rule of INR 15 lakh income for applying the 120 days period of stay threshold.
- Eliminating cascading effect on dividend declared by foreign company and business trust.
- Deferring the TDS and TCS provisions applicability on e-commerce transactions and foreign remittance/sale of any goods respectively to 1 October 2020.
- Enhancing of scope of equalisation levy.

Residential status

Indian citizens and Person of Indian Origin (PIO)

- The Finance Bill proposed to reduce the period of stay criteria for Indian citizens and PIO visiting India to 120 days from the existing 182 days.
- The Finance Act now provides that the above condition would apply only in case of those Indian citizens and PIO having total income (other than income from foreign sources) exceeding INR 15 lakh during the previous year.
- Further, such Indian citizens and PIO having period of stay exceeding 120 days but less than 182 days during the year shall be classified as 'Not Ordinarily Resident' (NOR).

Citizenship-based deemed residency

- It was proposed to introduce the concept of citizenship-based deemed residency for Indian citizens who are not liable to tax in any other country by virtue of residency, domicile or any other similar criteria.
- The provision is now amended to provide an additional condition that the concept of deemed residency would apply only to those Indian citizens having total income (other than income from foreign sources) exceeding INR 15 lakh during the previous

year. Further, such individuals shall be classified as NOR.

Condition for becoming NOR

- The Finance Bill also proposed to replace the existing twin conditions to determine the residential status for becoming a NOR with a new single condition i.e., individual or HUF whose manager is non-resident in India in seven out of 10 years preceding the previous shall be regarded as NOR.
- The Finance Act has not considered these propositions. Thus, the earlier twin conditions would continue for determining NOR.

Meaning of 'income from foreign source'

The Finance Act has defined this expression to mean income that accrues or arises outside India except income derived from a business controlled in or a profession set-up in India.

Dividend taxation

Clarification on dividend received after 1 April 2020

- The dividend distribution tax (DDT) was proposed to be abolished and replaced with the classical system of taxation with effect from 1 April 2020. Consequently, tax exemption of dividend received on or after 1 April 2020 was also proposed to be removed. This created an ambiguity regarding taxation of dividend that have been declared before 1 April 2020 but received by the shareholder after 1 April 2020.
- The Finance Act has now clarified that dividend received on or after 1 April 2020 on which DDT and tax[1], wherever applicable, has been paid shall continue to remain exempt.

Eliminating cascading effect

- The Finance Bill proposed to eliminate the cascading tax effect in case of inter-corporate dividends by providing a deduction in respect of dividends **received by a domestic company** to the extent such dividend is distributed.
- This has now been expanded to include **dividends received by a foreign company and a business trust.** Thus, deduction of dividend received from a foreign company or a business trust is also available.

[1] As per the provisions of section 115BBDA of the Income-tax Act, 1961

Business trust

The business trust shall be exempted in respect of income received as dividends from the special purpose vehicle ('SPV'), where such SPV has not exercised the concessional tax regime[2].

New provision relating to tax deduction at source (TDS) on cash withdrawal

- Under the erstwhile provision[3], banks[4] were required to deduct tax at source at the rate of 2% on cash withdrawal by a person ('the recipient') exceeding INR 1 crore in a previous year.
- The Finance Act has substituted the above provision with effect from 1 July 2020 and now provides as follows:
  - Withholding tax of **2%** on the entire amount of cash withdrawal if withdrawal exceeds INR 1 crore during the previous year.

  However, if the recipient who has not filed the tax return for the three preceding years (and the time limit for filing the return of income has expired, immediately preceding the previous year in which the payment is made), the provision of section shall apply as following:

  - TDS at the rate of **2%** where the amount or the aggregate of amounts paid during the year exceeds INR 20 lakh but does not exceed INR 1 crore.
  - TDS at the rate of **5%** where amount or the aggregate of amounts paid during the year is in excess of INR 1 crore.

TDS by e-commerce operator (ECO)

- The Finance Bill proposed to impose TDS at the rate of 1% on the gross amount of sales or service or both by an ECO on payments made to a resident e-commerce participant[5] from 1 April 2020.
- The Finance Act has deferred the provisions to 1 October 2020. In addition, the provisions have been amended:
  - ECO shall be deemed to be the person responsible for paying to e-commerce participants.
  - The Central Board of Direct Taxes (CBDT) has been empowered to issue

[2] As per provisions of section 115BAA of the Income-tax Act, 1961
[3] Section 194N as inserted vide the Finance (No.2) Act, 2019
[4] Including cooperative society engaged in carrying on the business of banking and a post office
[5] i.e. person selling goods and/or services on electronic or digital platform

guidelines to remove any difficulty in implementing the provisions.

Provisions relating to Tax Collection at Source (TCS)

Foreign remittance

- The Finance Bill proposed TCS at the rate of 5% on purchase of overseas tour programme package or on remittances of INR 7 lakh or more in a year under the Liberalised Remittance Scheme (LRS) route through an authorised dealer with effect from 1 April 2020.
- The Finance Act has deferred the applicability of such provisions to **1 October 2020**. In addition, the TCS rate has been reduced to 0.5% if the amount being remitted is a loan obtained in excess of INR 7 lakh from any financial institution[6] for the purpose of pursuing any education.

It has been clarified that the authorised dealer is not required to collect tax if the seller has already collected such sum.

Sale of goods

- The Finance Bill also proposed that a seller of goods shall collect tax on payments in excess of INR 50 lakh at the rate of 0.1% from the buyer provided the seller's turnover exceeds INR 10 crore. This provision was effective from 1 April 2020.
- The Finance Act has now amended this provision to state that such provisions shall not be applicable in case of goods exported out of India. Also, a person importing goods into India has been specifically excluded from the meaning of the term 'buyer'.
- Further, the applicability of such provisions has been deferred to 1 October 2020 and the Central Board of Direct Taxes (CBDT) has been empowered to issue guidelines to remove any difficulty in implementing the provisions.

Enlarging the scope of equalisation levy with effect from 1 April 2020

The Finance Act has proposed to expand the scope of equalisation levy. Such proposal was not covered in the Finance Bill.

- **2% equalisation levy** on the amount of consideration received or receivable by ECO[7] from e-commerce supply or services made or provided or facilitated by it to:

[6] As defined in section 80E

[7] means a non-resident who owns, operates or manages digital or electronic facility or platform for

- Person resident in India
- Non-resident in specified circumstances[8]
- Person who buys such goods or services or both using Indian IP address

- Equalisation levy to be remitted quarterly by 7th of month following the end of Quarter (31 March for Quarter IV)
- **'E-commerce supply or services'** means
  - online sale of goods owned by the ECO or online provision of services by ECO
  - online sale of goods or provision of services or both, facilitated by the ECO
  - Any combination of above

Equalisation levy not leviable:

- Where the ECO has a permanent establishment (PE) in India and the supply or services is effectively connected with such PE
- Where the equalisation levy is otherwise leviable
- Where the sales, turnover or gross receipts of the ECO from the e-commerce supply or services is less than INR 2 crore during the previous year.

Others

TDS on income in respect of units

Due to abolition of DDT, income from certain units is made taxable in the hands of the unit holder. In this regard, the Finance Bill proposed that the payer would be required to withhold taxes on distribution of income from units. The TDS provisions have now been amended to provide that TDS shall not be deducted if the income is in nature of capital gains.

TDS on royalty

TDS on Fee for Technical Services (FTS) was proposed to be reduced to 2%. The Finance Act has also extended the reduced TDS of 2% to royalty payments on sale, distribution or exhibition of cinematographic films.

Optional Personal tax regime for individual and Hindu Undivided Family (HUF)

The Finance Bill had proposed an optional personal tax regime for individuals and HUFs. It was stated that once the option is exercised by

online sale of goods or online provision of services or both
[8] Specified circumstances means sale of advertisement, which targets a resident customer or a customer who accesses the advertisement though Indian IP address; and sale of data, collected from resident person or from a person who uses Indian IP address.

the Individual or HUF having business income, it shall be applicable for subsequent years as well. Such person had the option to withdraw this option only once and thereafter, shall not be eligible to exercise this option unless the person ceases to have business income.

This led to an ambiguity on whether Individuals or HUFs earning 'income from profession', will also be covered by this provision. The Finance Act has extended this condition to individuals and HUFs earning 'income from profession'.

Exemption to sovereign wealth funds ('SWF') and wholly owned subsidiaries of Abu Dhabi Investment Authority ('ADIA')

The Finance Bill had proposed tax exemption from interest, dividend and long-term capital gains arising from investments in India by specified persons being SWF and wholly owned subsidiaries of ADIA.

The Finance Act now extends such benefits to investments made by foreign pension funds.

The scope of eligible investment is further expanded to include infrastructure investment trusts and Category-I or Category-II Alternative Investment Fund having investments in prescribed infrastructure facilities and business as notified by the central government.

Concessional tax regime

The Finance Bill had proposed to provide deduction from the total income in concessional tax regime[9] for inter-corporate dividends effective FY 2019-20. However, the Finance Act provides to make these provisions effective from FY 2020-21.

Our comments

The Finance Act has made attempts to address the anomalies/concerns raised by the stakeholders over the proposed Bill presented by the finance minister. The clarifications with regards to income threshold for residential status, stateless persons, providing dividend tax credit vis-à-vis foreign companies and business trusts, etc. is a welcome move.

[9] Section 115BAA and Section 115BAB of the Income-tax Act, 1961

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