Deloitte.

Budget expectations

November 2023

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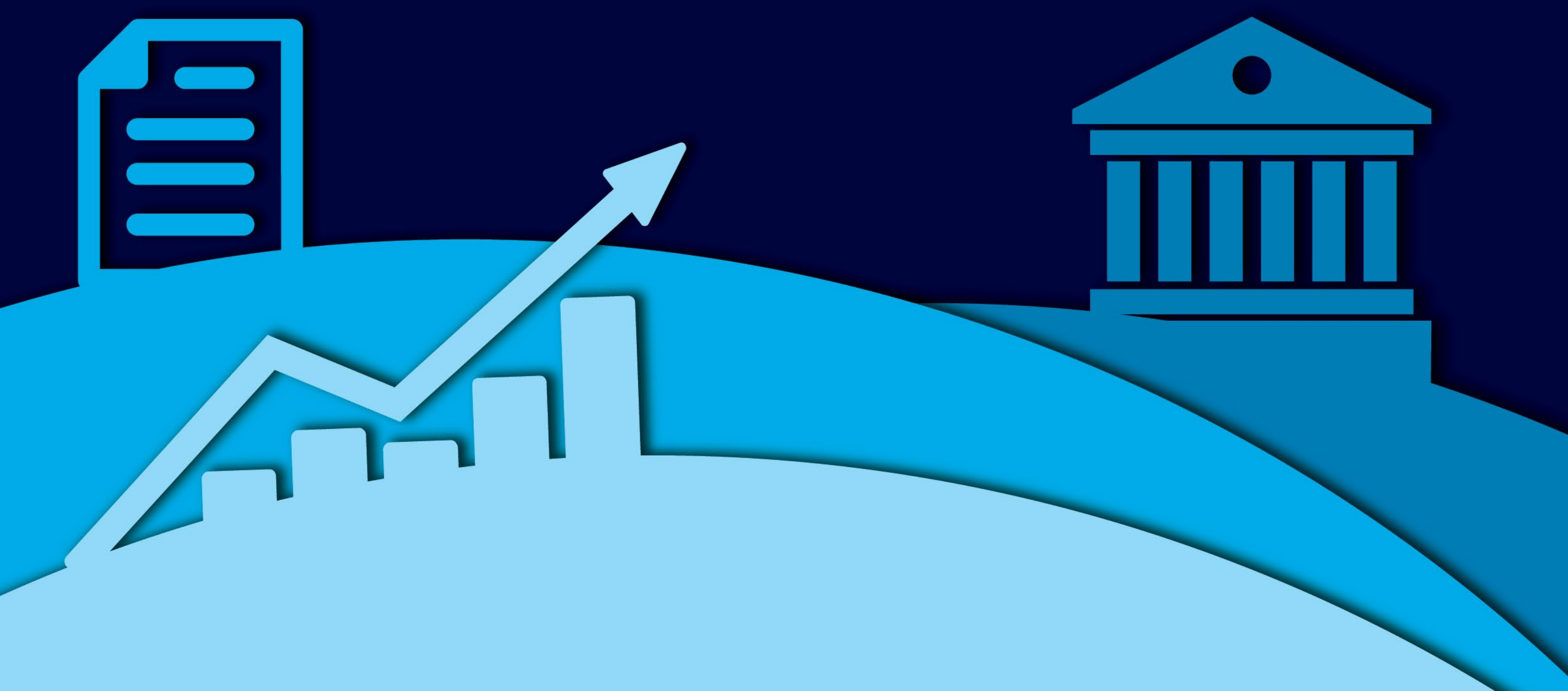
Policy and Economy



Policy & Economy

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Current environment

Upside risks

- Growth: India grew 7.8 percent in the first quarter; a large part of this growth came from strong domestic demand even during the global economic slowdown weighed on exports. Considering Q1 GDP growth, we have revised up our growth estimate for this year; growth is expected to be 6.5–6.8 percent for FY24. The IMF also revised up India's growth forecast to 6.3 percent for FY24. According to IMF estimates, the Indian economy will surpass Japan and Germany to be the world's third-largest economy achieving a GDP of US$ 5 trillion by 2027.
- Robust infrastructure spending: The government has been consistently increasing budgetary allocation for infrastructure. Capital expenditure is expected to grow from 22 percent in FY23, to 38.9 percent in FY24. The calibrated policy actions help improve logistics and supply chain.
- Credit growth accelerating: Consistent improvement in the bank's balance sheets over the past couple of years and the fall in NPAs across sectors have increased banks' willingness to lend. This has helped credit growth to recover quickly after the pandemic. Credit growth is the highest in the services sector, followed by growth in personal loans and loans to the industry.
- Recovering in the MSME sector: The sector is emerging out of the crisis after the pandemic; several parameters point to its steady growth. The demand for loans, for example, in the sector increased 33 percent in Q1 FY23-24, whereas delinquencies are declining as NPAs have improved across segments of MSME lenders and borrowers.

Downside risks

- Inflation: Concerns around rising prices are at the top of mind for policymakers. High food prices, especially double-digit growth in pulses and cereals, which have a significant share in the CPI food basket, are concerning. Moreover, oil prices started trending up quickly. Food and fuel prices are likely to keep inflation high. Despite the RBI raising rates to 6.5 percent since April 2022, inflation remained above its tolerance range.
- Elections: The upcoming national and key state elections in India over the next few months can create a policy pause for about three months until the new government assumes office. Policies around ensuring energy supplies, climate change, sustainable development, international trade, maritime, space and cyber-security, non-proliferation, and cross-border terrorism will be on priority for the incoming government.
- Geopolitical uncertainties: Geopolitical concerns are weighing on global investors and policymakers. As the Israel and Palestine war intensifies, there are fears that the regional dispute could prolong and have a contagion impact on global supply chains and the economy. The ongoing Israel-Hamas conflict could destabilise already tense steel and oil supply chains worldwide. Crude price of US$90/bbl will put further stress on India's current account deficit. Higher import bills and a slowdown in export growth amidst a global slowdown can push the trade deficit high.
- Diverging demand gaps: Consumer spending has seen a strong revival after the pandemic in the high-income segment. Services such as travel and hospitality, and sale of high-end vehicles in the passenger vehicle segment have seen a surge,

pointing to pent-up demand amongst the top income percentile of the population. However, rural demand has not yet seen sustainable growth. Segments such as FMCG, entry-level auto segments, and two-wheelers are yet to pick up sustainably. Simultaneously, rising policy rates have put pressure on household borrowings as EMIs have gone up. Spatial and erratic monsoon has further added to stress on rural spending abilities.

Expectations

- Despite a slowdown in the global economy and uncertainties, India's growth outlook remains positive. The IMF recently upped its projections for India this year. We also remain optimistic about the economy this year and expect India to grow between 6.5 percent and 6.8 percent during FY2023–24 in our baseline scenario, followed by an average of 6.65 percent and 7.95 percent over the next two years as the global economy turns buoyant. India will have to rely on its own domestic demand to drive its growth, specifically, private consumption and investment spending. However, inflation could affect stability in growth. We expect higher prices over the next 1.5 years; prices are expected to remain in the upper range of the RBI's inflation target band over the forecast period.

Top asks

- **Expectation #1**
  - Over the past five years, the government has focused on building a strong infrastructure. Infrastructure spending as a percentage of GDP increased from 1.13 percent in FY 2019-20 to a budgeted estimate of 3.3 percent of GDP in FY 2023-24. Given the strong forward and backward linkages in the sector, spending helps support rural income and jobs; it is also likely to improve logistics costs. However, most spending is concentrated on roads and railways. On the other hand, over the past two years, spending on urban development and energy as a share of GDP has declined.
  - The government is expected to divert some of its expenses towards improving the port and shipping; energy, especially green and sustainable energy; and urban infrastructure. In this budget, the government's focus should be on the transition from carbon-dependent to energy-efficient policies.
- **Expectation #2**
  - To date, the public sector drove the maximum investment, while the private sector had a modest share. In a few sectors, investments have taken off faster than others. Global uncertainties and modest consumer spending have kept private investors at bay. A higher capex spending by the government is expected to crowd in capital spending. That said, it will require some government incentives and a few measures in this direction.
- **Expectation #3**
  - In GDP, export growth contracted by 7.7 percent in 1Q FY24 after growing in double digits for the eight consecutive quarters. As the slowdown was largely driven by deceleration in growth of major economies, boosting exports in diversified and new markets, while helping existing markets grow, is important.
- **Expectation #4**
  - Subsidies, as a percentage of budgetary outlay, are likely to be about 7 percent during FY 2023-24, down from 8 percent in FY 2022-23. This will help bringing down the fiscal deficit as the government consolidates its spending. However, lower subsidies can put pressure on rural demand amidst challenges such as lower agriculture output. The government is expected to divert savings from subsidies towards spending that can support sustainable growth in income amongst rural households, boosting the rural economy's disposable income. One of the ways could be higher spending on building rural infrastructure or providing incentives that improve cash flow.

Policy recommendations

Recommendation #1

In line with the expectations, we recommend incentives such as broadening the scope of PLI schemes to sectors such as chemicals and services that create demand for more manufacturing.

Recommendation #2

The government can help provide funds for the Remission of Duties and Taxes on Exported Products (RoDTEP) and other export promotion initiatives.

Sectors

Agriculture

Anand Ramanathan
Partner and Consumer, Products and Retail sector Leader

Current environment

- India is an agrarian economy with the agriculture and allied sectors being the largest source of livelihood.[1] In FY23, the estimated Gross Value Added (GVA) for the sector reached **~US$ 275 billion,**[2] contributing ~15 percent to the total GVA.
- The country's agricultural export reached **US$ 53 billion**[3] in FY2023, up ~6 percent from FY2022. Rice, marine products, and sugar are the top three contributors.
- Agriculture in India is slowly shifting from traditional farming to horticulture, dairy, poultry, fisheries, and processing. With rising income levels, urbanisation, and changing consumption patterns, the demand for fresh, higher nutritional, and processed food is increasing in rural and urban households.
- Farmers have also moved up in the agri-value chain. They plan to adopt modern farming techniques (crop diversification, crop mapping, precision farming, polyhouses, breed improvement in dairy, drones, etc.) to reduce manual efforts and increase returns. For example, large farmers in UP traditionally growing rice and wheat have diversified into fruits, dairy, poultry, and exotic crops, such as strawberries and dragon fruit. Further, increasing interest from start-ups and private players has led to better prices and innovative solutions. Interventions such as farm-to-fork models enable farmers to access markets offering better prices and reduce crop wastage.
- Despite an increase in demand and supply, the sector needs to address key challenges, such as climate change, fragmented landholdings, rising input costs, mechanisation, and market linkages.
- To support the sector, the government has already made massive strides through its policies, schemes, and initiatives. In addition to existing schemes, such as PM Matsya Sampada Yojana, the Production Linked Incentive (PLI) scheme, and Krishi UDAN 2.0, the government recently announced the development of a Digital Public infrastructure for agriculture to enable farmer-centric solutions. It also announced an Agriculture Accelerator Fund to encourage agri-start-ups in rural areas and the Atmanirbhar Clean Plant Programme to boost the availability of quality planting material. Further, the government needs additional measures to increase digital adoption; strengthen the food processing value chain, post-harvest infrastructure, market linkages, and regulations around land pooling; and ensure ease of doing business and investment support.

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[1] IBEF-Agriculture and Allied Industries, May 2023
[2] NABARD- https://www.nabard.org/pdf/2023/the-year-in-context-eng.pdf
[3] NABARD- https://www.nabard.org/pdf/2023/the-year-in-context-eng.pdf
[4] Technology- https://inc42.com/resources/what-does-2023-hold-for-indian-agritech-industry/

Expectations

Top asks

- **Expectation #1: Increasing digital adoption**
  - The tech-powered agriculture industry is expected to reach a valuation of **US$ 13.5 billion[4] by 2023.** Additionally, the role of **AI in agriculture** is anticipated to reach **US$ 4 billion by 2026.[5]** Increased adoption of tech-driven modern agricultural practices, such as crop mapping, precision farming, breed improvement in dairy, automation of poultry farms, and drones, are likely to enhance efficiency and empower farmers to help them make informed decisions. However, due to lack of awareness, presence of segregated small-farm holders, and access to credit and other factors, digital adoption is still at an emerging stage in India. The government recently announced the development of Digital Public Agriculture Infrastructure and an Agriculture Accelerator Fund (AIF), to foster farmer-centric solutions, nurture agri-tech growth, and encourage agri-start-ups in rural areas. Further, the government should aim to increase digital adoption by suitable interventions focusing on educating stakeholders, improving tech affordability and accessibility, increasing investments in R&D, etc. Robust data collection and analysis systems should be established to provide farmers accurate information on market trends (on price, exports, etc.), weather patterns, and best practices. Steps should be taken to strengthen public-private partnerships for increased adoption of digital technologies.
  - Ag-tech players help drive margin across the agri value chain. Technologies, such as geographical mapping and real-time updating of cold storage capacity, can enable farmers to save time and transportation costs. **Drones and AI** use can help create agricultural yield prediction models to track soil and crop health. Similarly, **precision agriculture** can help enhance yield by ~30 percent and reduce input costs by ~20 percent.[6]
  - Digital techniques, such as smart irrigation, soil health monitoring, and remote sensing, facilitate better data access, informed decision-making, and efficiency.

- **Expectation #2: Strengthening food processing value chain**
  - The Indian food processing market is estimated to reach **US$ 535 billion[7] by 2025** at a **CAGR of ~15.2 percent** (five years). Additionally, exports of processed food products reached ~US$ 20 billion in nine months of FY23, a jump of ~13 percent.[8] With total FDI between **April 2000 and December 2022 at ~US$ 12 billion,[9]** the sector witnessed an influx of investments offering higher value to agricultural produce, limiting post-harvest losses, rising employment opportunities, etc. The government has already taken measures to boost the sector through its schemes, policies, and incentives such as the Pradhan Mantri Kisan Sampada Yojana (PMKSY) and Pradhan Mantri Formalisation of Micro Food Processing Enterprises Scheme (PMFME). With growing allied sectors, changing consumption patterns, and rising need for employment creation, the food processing value chain needs strengthening. Thus, the government should promote the cluster development and creation of micro-processing units across states.
  - Establishing clusters and micro units will increase processing output capacity and reduce unnecessary costs. Clusters can enable multiple food processing units to share common infrastructure and services, thus helping reduce input and other costs and facilitate demand-driven processing. With high quality, supplying capacity clusters as one unit can have wider market access and promote collaborations and exports. Farmers and Farmer Producer Organisations (FPOs) should be encouraged in setting up micro-processing units under schemes such as Pradhan Mantri Formalisation of Micro Food Processing Enterprises (PMFME). This can help farmers and FPOs gain an additional income or a premium on their produce. For example, dairy farmers can produce curd, paneer, sweets, etc. Similarly, fruit farmers can supply pulp, juices, etc. However, quality measures should also be strictly enforced, to ensure wider acceptance in the domestic and international markets.

- **Expectation #3: Improving post-harvest infrastructure**
  - In India, post-harvest losses are **~10–25 percent for perishable** foods, such as milk, fish, and eggs, and **~30–40 percent for fruits and vegetables.[10]** Increasing and improving storage and grading facilities and transportation

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[5] AI in Agri- InC42- https://inc42.com/resources/what-does-2023-hold-for-indian-agritech-industry/

[6] FICCI- https://blog.ficci.com/archives/8485

[7] Processing- https://www.investindia.gov.in/sector/food-processing#:~:text=By%202025%20the%20Indian%20Food,to%20%246%20Tn%20by%202030.

[8] https://pib.gov.in/PressReleasePage.aspx?PRID=1897723

[9] https://www.investindia.gov.in/sector/food-processing#:~:text=By%202025%20the%20Indian%20Food,to%20%246%20Tn%20by%202030

[10] Post-harvest- https://write.agrevolution.in/reducing-post-harvest-losses-157e60cc4d0

networks will reduce post-harvest losses and enable timely transportation of quality produce. Further, it offers higher value to agri produce and enhances key stakeholders' revenues. The existing Agriculture Infrastructure Fund (AIF), Mission on Integrated Development of Horticulture (MIDH), and other schemes should be used to improve infrastructure capacities across states. The government should encourage the creation of multi-commodity cooling and grading centres near mandis, solar-powered micro-cooling units, and cooling units near airports and ports, etc.

- Creating multi-commodity cooling near mandis and airports can enable farmers to sell their produce at a better price, cut transportation costs significantly, and avoid distress selling. Additionally, grading facilities near mandis will help farms yield better prices for every commodity they sell. Cooling units near ports and airports across states can ensure quality as the commodity is not stored in refer vans until it is exported. Further, interventions such as solar-powered cooling units specifically in rural areas will promote agri-preneurship and work as an efficient model to reduce post-harvest losses. Farmers can use these solar-enabled cooling units to hold their produce and sell at the right time by paying nominal charges.

- **Expectation #4: Boosting the export ecosystem**
  - India's agricultural export reached US$ 53 billion in FY2023.[11] Rice (US$ 11 billion), marine products (US$ 8 billion), and sugar (US$ 5.8 billion) were the top three contributors. This milestone was achieved because of well-crafted trade policy interventions, effective execution, and various initiatives. As the increase in agricultural exports leads to higher earnings for farmers and positively affects their income, the government should take some focused measures to boost the overall exporting ecosystem. Some of these measures are mentioned below.
    - **Demand mapping:** Based on regular identification of markets, farmers should be encouraged towards demand-driven production, to ensure demand-focused supply.
    - **Strengthening post-harvest infrastructure:** Improve infrastructure by setting up cooling units near airports and ports to improve quality. Moreover, establish a digitally enabled supply chain to track agri and allied produce. This helps in demand mapping.
    - **Quality assurance and standards:** Foster adherence to country-specific compliances and benchmarks per global standards for increased acceptance of produce.
    - **Export promotion:** Incentivise the promotion of agricultural exports to make domestic produce a brand in the global market.

Policy recommendations

- **Recommendation #1 –** Move towards digital adoption aim: The government should focus on last mile reach of the benefits of 'Agristack' as Agristack aims to furnish real-time and accurate data regarding markets, schemes, logistics, warehousing, and market access (e-NAM and marketing channels). This integrated ecosystem should function as a comprehensive repository of farmer information, encompassing data on soil conditions, crop specifics, and land records, accessible across different states. The government should also encourage state-level resource centres to support Agristack through data, production, prediction, analysis, farmer/FPO details, crop insurance, etc.
- **Recommendation #2 –** Improve post-harvest infrastructure: The government should encourage the creation of storage, grading, and cooling units near mandis, airports, etc. Under AIF and similar schemes, the government can incentivise development of these units. Further, capacity building at these locations will foster grade-based pricing of produce, reduction in transportation cost, and a decline in distress selling.

[11] NABARD Annual Report 2022-23

Education

Kamlesh Vyas
Partner

Regulatory

Current environment

The regulatory landscape for the education sector is evolving rapidly. From taking measures and internationalising the education ecosystem to bringing in transparency and industry relevance, regulators are enabling opportunities for stakeholders through regulatory changes.

International Financial Service Centre Authority ("IFSCA") regulations were introduced to enable foreign universities to set up their campuses in GIFT City and offer finance and STEM-related programmes to students in India. These regulations enable the framework to promote joint/dual degrees and introduce other similar initiatives to encourage internationalisation.

Some areas where regulatory stakeholder consultations are either impending or have already been implemented are likely to bring about significant improvements in educational outcomes. These areas are mentioned below:

- UGC guidelines to enable the setting up of foreign university campuses anywhere in India; this will further add to the impetus of internationalisation
- Institutional development plan for higher education institutions that will provide a strategic roadmap for functional and structural growth of institutions
- Mandatory disclosures on institutions' websites that will bring in the much-needed transparency and provide the base for making a considered decision on admissions by students and parents
- Introduction of internships at an undergraduate level, which will help upskill students and make them employment-ready

Although NEP 2020 provides a broad framework and policy direction, its timely implementation is critical to the sector's growth. The National Research Foundation is one such initiative that would help enhance research capabilities and the infrastructure required to undertake research in the country. This is one of the most significant contributors to the development of the innovation landscape in the nation.

Expectations

Top asks

- **Expectation #1: Enable foreign investments and foreign currency loans**

  In the sector, 100 percent FDI is allowed under the automatic route. However, given the entity's sectoral requirements to act as a "Trust" or "Society", FDI in such entity types is restricted. Similarly, raising foreign currency loans (at cheaper rates) is not allowed if the borrowing entity is a "Trust" or "Society".

  – With transformation needs required for better student learning and engagement, as well as to stay relevant, educational institutions need to upgrade their infrastructure and adopt newer and better technology solutions for the delivery of programmes. They also need to continuously reskill their faculty and hire new faculty members for new-age skill sets. These initiatives require institutions to raise funds. Domestic banks do not consider lending to institutions favourably due to lack of transparency in their entity structure of "Trust/Society" and related governance.

- An amendment to the exchange control regulations should be made to allow foreign investments and availment of foreign currency loans in "Trusts and Societies" running educational institutions. The 2021 Union Budget recommended enabling FDI and ECB for the educational sector. However, action is yet to be taken.

- **Expectation #2: Expediting clearances for receipt of donations and grants from foreign sources**
  - Receipt of grants and donations (including those for conducting joint research programmes with overseas institutions) from foreign sources is an important source of income for educational institutions. Such receipt of grants or donations needs prior permission or registration with the Ministry of Home Affairs. This process takes quite a bit of time.
  - Defined timelines for obtaining clearances from the Ministry of Home Affairs must be outlined and the process should be streamlined.

- **Expectation #3: Introduce flexibility of receiving student fees in Indian rupees by foreign education institutions set up in GIFT City**
  - The IFSCA (setting up and operation of International Branch Campuses and Offshore Education Centres) Regulations, 2022 require the transactions to be undertaken by educational institutions, except defraying administrative expenses, only in foreign currency.

    The fee payment by students would also need to be done in foreign currency. The conversion charges of which add to the financial burden on students/parents.
  - An exemption should be given for students to pay their fee (academic, hostel, and other similar payments) in the Indian currency.

    A similar exemption had been issued by RBI allowing units in IFSCA to conduct business in INR vide FEMA Notification No. 397/RB-2020, under the Foreign Exchange Management (International Financial Services Centre) (Amendment) Regulations, 2020.

    This would ease the financial burden on students/parents on account of foreign exchange conversion charges.

Other policy recommendations and expected impact

- A fast-track process for the application and grant of patents for educational institutions should be introduced. Grant of patents is a sign of innovation. With reduced timelines for the application process and its grant, it will lead to higher research and development in the country.
- Minimum area requirements to set up higher educational institutions should be done away with and a lease-based model (as opposed to ownership of land) should be introduced. This could help reduce capital requirements for new institutions, considering the constraints posed by the paucity of funds in the higher education ecosystem. It would allow prioritizing funds allocation towards improving infrastructure, hiring quality faculty, enhancing student experience, and launching new-age industry-relevant programs.
- The eligibility condition for a foreign university to set up a branch campus in GIFT City, from a QS top 500 university to a top 500 university per any global ranking system, should be revised. This would increase the number of universities eligible for applying to set up a campus in GIFT City.
- The validity period of a certificate of registration by GIFT City to foreign education institutions should be removed. Educational institutions are set up on a strategic and long-term basis. The process for renewal every five years causes administrative inconvenience.

- **Continuation and stabilisation of the current policy intent**
  - On several areas, there may not be any major changes in the education Budget this year. This is based on large-scale changes, such as NEP 2020, NCF, NRF, and PM e Vidya, over the past few years. The government may look at stabilising their implementation before directional changes or new initiatives/schemes are announced in the next few years. The funding support for ongoing schemes, such as Samagra Shiksha Abhiyan and PM Shri Schools, is likely to continue.
  - There may be additional funding to integrate Bal Vatikas and Anganwadis with primary schools and for training teachers.
  - In higher education, universities may receive support to transition to Multi-Disciplinary Education and Research Universities (MERU), to implement the Academic Bank of Credit (ABC) system, to establish campuses abroad, and to enhance the Gross Enrollment Ratio (GER).

Direct tax

Current environment

On the direct tax front, the education/not-for-profit space has seen increased vigilance with restrictive provisions introduced under various Acts, such as The Income-tax Act, 1961 ("IT Act"). For example, provisions introduced for specified violations and enabling provisions to tax income are not in compliance with prescribed exemption provisions.

This has led to the increased compliance burden on taxpayers. The increased compliances are expected to make way for simplified, comprehensive compliances, while maintaining the required level of monitoring/oversight.

Expectations

Top asks

- **Expectation #1: Clarification in relation to meaning of the term "education" for purposes of Section 11 and 10(23C)**
  - In October 2022, the Hon'ble Supreme Court ('SC') in the case of *New Noble Education Society [TS-809-SC-2022]* interpreted the meaning of the term "education" in a restrictive manner by ruling that IT Act provides for "imparting formal scholastic learning" as a meaning to the word "education" under the definition of "Charitable Purpose" under Section 2(15).

    In the progressive world, educational institutions are expected to educate, teach, and train persons in various skills to help them compete with similar experts worldwide and increase their employability. The move will ensure the availability of skilled manpower for futuristic technologies and high-end manufacturing and research, along with helping in capacity building of the nation.
  - In light of current dynamic environment and changes in social and economic conditions, the meaning of "education" should be broadened to include systematic dissemination of knowledge (through regular classes, attendance requirements, and enforcement of discipline) and training in specialised subjects.

- **Expectation #2: Clarification in relation to a period of applicability of equalisation levy**
  - The 2 percent equalisation levy was introduced in 2020, bringing the online presence of various foreign education institutions under the tax net. While further clarifications were introduced in 2021, institutions across the world continued to face challenges on determining their applicability considering the widely worded provisions

    In October 2021, India and the US agreed on a transitional approach ("Joint Statement") whereby applicability of equalisation levy was agreed to be restricted until the implementation of Pillar One or 31 March 2024, whichever is earlier.
  - In line with the above, a suitable provision may be incorporated in law to restrict the applicability of equalisation levy up to 31 March 2024. Further, the transitionary measures as mentioned in the joint statement should be suitably incorporated in law.

- **Expectation #3: Clarification in relation to tax implications/incentives to foreign universities**
  - At present, regulations have been introduced in relation to the manner/procedure to be followed by foreign universities/educational institutions for setting up International Branch Campuses (IBC)/Offshore Educational Centre (OEC) (including relevant conditions to be satisfied).
  - Certain key clarifications ought to be provided from a tax perspective as mentioned below:
    - Most foreign universities get perpetual tax exemption in their home countries. Hence, to incentivise the top universities to set up under IFSCA, a similar perpetual tax exemption ought to be provided. A perpetual tax holiday would prove more attractive and at par with the tax exemptions in the home country. Section 80LA, which currently provides a tax holiday for 10 years, may be amended to this effect to provide the perpetual exemption, subject to satisfaction of condition as may be laid down.
    - Foreign players may not find it helpful if clarifications were provided that prescribed transactions/interactions by the IBC/OEC in India shall not result in a "Significant Economic Presence" and consequent business connection.

Technology, media & telecommunications

Peeyush Vaish
Partner and TMT Industry Leader

Expectations

Transfer Pricing

Expectation #1: Streamline the Advance Pricing Agreement (APA), Mutual Agreement Procedure (MAP) regulations

- As of March 2023, about 1,659 APA applications have been filed, with 516 APA applications conclusions. To resolve backlog of more than 1,100 applications and manage the load of new applications expected to be filed, the government should increase the bandwidth of the APA workforce.
- Most APA applications that culminated into agreements, pertain to the service sector. A majority of these, in turn, are captive companies involved in software development and Business Process Outsourcing (BPO). Some of these companies are also involved in engineering design services, research and development, and Knowledge Process Outsourcing (KPO). In relation to these, the following recommendations should be taken into consideration:
  - For subsequent applications, the government should release a standard readiness questionnaire; on the basis of which, APAs may be speedily concluded with Central Board of Direct Taxation (CBDT).
  - For applications already filed and pending with APA authorities, a list of standard data points should be released. Based on those data points, pending APAs may be concluded speedily.
- Fixed timelines should be prescribed for the closure of APAs for transactions where a significant number of APAs are already concluded (such as provision of ITeS and software development services).
- A Permanent Establishment ("PE") of an Indian company, located outside India, is subject to transfer pricing provisions in the country where the PE is located. In the event of any dispute with the foreign country's tax authority, such PE may have recourse to Mutual Agreement Procedure restoration as provided in the treaties between India and another country. To provide forward looking tax certainty to such PEs, the scope of APA provisions should also be widened to include recourse to bilateral APAs between India and another country where the PE is located.
- Single-owner Limited Liability Companies (incorporated under the US laws) is enabled to claim the treaty benefits for the purpose of APA/ MAP applications.

Expectation #2: Royalty payments for use of technological capabilities, know-how by Indian companies engaged in manufacturing and distribution business of foreign technology products/services

- Indian companies engaged in the manufacturing and distribution of foreign technology products/services, usually pay royalty for using technological capabilities, know-how, etc., to the owner of propriety technologies. Such technological capabilities and know-how are essential to conduct business in India. As part of the arrangements, often, the technology proprietor is issued equity or other forms of remuneration by the Indian company, as consideration for receiving the technology. To attract further investments in technology and encourage investments in the technology sector, guidance/ notification should be issued to field officers on mechanisms to review such transactions.

Expectation #3: Ensure consistency in compliance requirements for income tax return and transfer pricing compliance requirements for non-resident taxpayers

- The Finance Act of 2020 granted exemption to non-residents under section 115A from furnishing a return of income in India in respect of specific income, such as royalty, fee for technical services, and interest, dividend, provided appropriate tax is withheld under the Indian Income-tax Act, 1961, on such income at the time of payment. However, similar relief was not granted in respect of such income to non-residents for TP compliance obligations, namely, furnishing Accountant's Report in Form No. 3CEB and maintenance of TP documentation. The Indian government should amend section 92E of the Act, to provide exemption to non-residents, similar to section 115A.

Direct Tax

Expectation#1: Provide clarity on the meaning of the term “Online Game”

- In a digital era, it is common to see online platforms luring customers by offering promotional schemes, such as spin the wheel or scratch card, on completing a prescribed number of transactions. The intention is to market a product/service offering and not participate in a typical game with the intention to win.
- Clarity should be provided by way of a circular capturing activities referred as “online game.” Else, all sectors offering and running marketing and promotional schemes/contests online, might get severely affected with the burden of discharging withholding tax obligation under Section 194BA.

Expectation #2: Provide clarity on taxation of telecom services in the hands of non-resident telecom operators

- Indian telecom operators make payment to foreign telecom operators for various telecom services. These payments were alleged by the Indian Revenue Authorities, as payments for using equipment/process and therefore, held as taxable, being in the nature of royalty.
- In a recent ruling of Vodafone Idea Ltd., Karnataka High Court held that payments made to foreign telecom operators for inter-connectivity use and bandwidth charges are not in the nature of royalty, as no right-to-use equipment is being provided by foreign telecom operators. A similar view has been pronounced in a plethora of rulings.
- Clarity is brought out in Income-tax Act, 1961 that payment for telecom services is not chargeable to income tax as they do not entail payment for using equipment/process.

Expectation #3: Increase in scope of provisions dealing with carry forward of losses and unabsorbed depreciation

- Benefit of carry forward of losses and unabsorbed depreciation is not available in case of amalgamation of companies not owning an “industrial undertaking”. The term “industrial undertaking” is defined to mean any undertaking engaged in the manufacturing or processing of goods, manufacturing of computer software, the business of generation or distribution of electricity or any other form of energy, the business of providing telecommunication services, whether basic or cellular, including radio paging, domestic satellite service, network of trunking, broadband network and internet services, mining or the construction of ships, aircraft, and railway systems.
- Consolidating entities within an industry helps in rapid growth and generation of substantial employment opportunities. This will in turn help make India a competitive country for foreign investment. To promote such consolidation, the benefit under Section 72A to carry forward loss and depreciation on amalgamation, should be extended to include other capital-intensive sectors. These sectors include media/broadcasting and entertainment, and infrastructure/capital-intensive service sectors, such as telecom infrastructure service provider and direct-to-home operators.

Indirect Tax

Expectation #1: Exemption on GST TCS obligations on e-commerce operators on facilitation of zero-rated supplies (exports)

- E-commerce has transformed the way business is done in India. The e-commerce industry has been directly affecting MSMEs in India. It has generated a favourable cascading effect on other industries.
- At present, per section 52 of the CGST Act, an e-commerce operator is required to collect GST TCS @ 1 percent of the net value of taxable supplies made through it by other suppliers where the consideration with respect to such

supplies is to be collected by the operator. Taxable supplies do not include exempt of NIL-rated supplies but includes zero-rated supplies. Given this, essentially, even when there is no GST liability payable on zero-rated supplies under an LUT, e-commerce operators are required to collect GST TCS in the absence of any separate GST collection by suppliers. The supplier is required to subsequently claim a cash refund of such GST TCS collected by the e-commerce operator. This results in cash flow issue for exporters and an increase in compliances for e-commerce operators and suppliers engaged in exports.

- The government should come forward with suitable amendments to exempt GST TCS obligations on e-commerce operators on facilitation of zero-rated supplies, to help with the cash flow issue for exporters and facilitate the ease of compliances.

Expectation #2: Investment-driven growth in the emerging space sector to support "Make in India"

- Production Linked Incentive (PLI) schemes are designed to incentivise domestic production and attract investment by providing financial incentives to manufacturers based on their output.
- The Indian private space sector, which is in a nascent stage, requires tax and policy support to boost manufacturing and spur research and development.
- PLI schemes for space tech start-ups are needed to help boost local manufacturing and encourage capability building within the country.

Expectation #3: Aligning classification and eligibility for concession under Notification No. 57/2017 dated 30 June 2017 for telecom products and equipment

- Notification No. 57/2017 grants concession to various telecom products and equipment. The benefit of concessional duty in some cases is granted based on technology-related descriptions. To ensure that such technology-related descriptions are better understood by various stakeholders, the Central Board of Indirect Taxes (CBIC), in consultation with the Department of Telecommunication (DoT), issued a circular in 2023, specifying the identification of the products/equipment.
- However, the industry continues to face coverage and eligibility-related interpretation issues, highlighting a need to suitably amend or issue clarification to address such issues. Let us look at a few examples.
  - According to the notification, Voice Over Internet Protocol (VOIP) phones falling under HSN 8517 62 90/8517 69 90 are excluded from the purview of concessional duty benefit. However, there are judicial precedents where VOIP phones have been classified under different tariff entry i.e., 8517 18. This causes undue hardship to the industry. Hence, the reference to VOIP should be removed from the specified entry in the said notification.
  - Carrier ethernet switches are ineligible for benefit of concessional duty. Typically, the difference between carrier ethernet switches and non-carrier ethernet switches is determined by their features and use. Several times, a non-carrier ethernet switch is treated by customs field formation as a carrier ethernet switch, thereby making it ineligible for concessional duty benefit. To address the said issue, CBIC should consider a certificate issued by a renowned agency/committee (such as the Telecommunication Engineering Committee) as a document based on which benefit under the notification shall be granted to non-carrier ethernet switches.
  - Multiple Input/Multiple Output (MIMO)/Long Term Evolution (LTE) products, according to the notification, are ineligible for benefit of concessional duty. Typically, MIMO/LTE-based technology is used in several IT equipment/telecom. The list provided in the circular is illustrative and inclusive in nature. As the list of MIMO/LTE products is not exhaustive, this may lead to disputes on concessional benefit. Hence, CBIC should issue an exhaustive list to eliminate the scope for any dispute of interpretational nature.

Personal Tax

Expectation #1

- TCS on overseas remittance for participating in employees' stock option plan should be discontinued if taxes are already deducted under section 192.

Expectation #2

- The employer should be permitted to claim foreign tax credit at time of withholding taxes under section 192, on salary income.

Consumer Industry - (FMCG, retail)

Anand Ramanathan
Partner and Consumer, Products and Retail sector Leader

Current environment

India's consumer industry is witnessing massive transformation and set to become the world's third-largest by 2027, only behind the US and China. Being one of the world's largest retail markets, India is expected to reach US$ 1.41 trillion by 2026.[1]

India is poised to welcome more than 900 million new internet users by 2025,[2] underpinned by affordable data plans and access to e-commerce, significantly altering purchasing patterns of Indian consumers. Consumer protection is gaining momentum as an imperative for the government and industries. Key driving forces behind this expansion include the increasing young population and a burgeoning middle class, predominantly concentrated in urban hubs. The middle class is the key stimulants of consumer demand and increasing expenditure. The business landscape is being reshaped with an emphasis on "experience" emerging as a pivotal factor influencing consumer preferences. While India's consumer industry is witnessing an exponential expansion with the increasing young population and relatively progressive purchasing power amongst the population, there remains disparity in terms of consumption between the urban areas and rural areas.

The focus has been on simplifying the tax structure and rationalise provisions. Moreover, the need of the hour is to provide certainty and visibility to taxpayers by clarifying ambiguous provisions and offering incentives to boost investments. Introduction of alternative dispute resolution mechanisms, such as Safe Harbour and APA, has strengthened the trust between the government and foreign businesses investing in India.

Expectations

Expectation #1: Promote investment and control in lation

(i) Support retail growth by taking steps to control inflation and increasing consumption

The country's retail inflation, measured by the Consumer Price Index (CPI), cooled to 5.66 percent in March 2023. Inflation data on the Wholesale Price Index (WPI) (calculates overall prices of goods before selling at retail prices) eased to 1.34 percent during the period. In 2022, CPI hit its highest of 7.79 percent in April 2022; WPI reached its highest of 15.88 percent in May 2022. We could anticipate some schemes such as Pradhan Mantri MUDRA Yojana Scheme gaining focus, as they could be a good avenue to provide financial support to small-scale kirana, and brick-and-mortar stores.

As the pandemic pressure receded, we saw challenges emerge in the form of high inflation. This pushed up commodity prices to multi-decade highs in many countries, causing central banks to raise interest rates and slow down economic activity. The prevalence of inflationary conditions had an impact on consumer behaviour, leading individuals to be more frugal with their spending. This in turn, resulted in a slowdown within the consumer goods industry.

[1] TOI
[2] Live Mint

Directly visible measure will be improvement in the country's consumer inflation index. The consumer inflation has been trying to correct itself for the past three quarters. However, due to challenging international landscape pushing fuel prices to record levels, combined with strained geopolitical conditions in the Middle East, Ukraine, and Russia, containing the rising prices of even basic food items in India have become challenging.

(ii) Foster more avenues of global investments in retail, including food retail

India is poised to attain a remarkable US$ 850-billion status within the grocery and food retail segment by 2025.[3] Given the immense potential of this sector, the government should revamp FDI policies, making them more attractive to investors and eliminating regulatory obstacles that have hindered foreign investment in the country.

At present, the government allows 100 percent FDI in food retail trading, including e-commerce, for food products manufactured and produced in India; this is subject to the government's approval. Expansion to other products manufactured in India would make the sector even more appealing to foreign investors, thereby generating more investments in the value chain.

The government should consider allowing 100 percent FDI in multi-brand retail trade at least for products manufactured in India, addressing existing barriers to push for a seamless growth and for harmonious coexistence of traditional and modern retail. In this regard, implementing a unified national policy is crucial.

(iii) Increased investment on Open Network for Digital Commerce ("ONDC") and digital network creation

The digitisation wave is yet to be seen in the digital commerce front. The launch of ONDC is planned to address that part of the economy. The government will keep investing in digital public infrastructure to drive digitisation in the Indian economy. India could see digital consumption surge five-fold to reach US$ 340 billion by 2030, with 500 million digitally transacting consumers. The network could be broader, with digital penetration across B2B companies reaching 8–10 percent. It could emerge as a more inclusive network with the scope to connect 80–90 million self-employed workers with demand and bring six-to-seven times more MSMEs into a buzzing, diverse ecosystem.[4]

Business-to-business sellers lag behind the global average of 20 percent when it comes to digital penetration in India. Of the 165–190 million consumers[5] who already use digital commerce, a much smaller number (10–15 million) are power users, typically living in urban areas and shopping across sectors.[6]

Only 6 percent of MSMEs, for instance, actively sell on e-commerce platforms. To boost digital commerce, the government must reimagine it, with an ecosystem that eliminates or resolves challenges for stakeholders.[7] Thus, a continued and significant investment in ONDC and digital infrastructure building is required for the country, to open a new fold of growth in the Indian economy.

Expectation #2: Strengthening rural consumption

Due to substantial rural unemployment rate and slow growth pace, expectations from the government to foster rural demand include continuation of policies such as increasing Minimum Support Prices (MSP) for agricultural produce, sustained investments in rural infrastructure projects, efficient implementation of Direct Benefit Transfer (DBT) schemes, and promoting robust crop sowing practices.

The government's thrust on capital expenditure and private-sector manufacturing and service activity should also support income generation and bolster economic activities. The focus should be on the local implementation of government policies. This creates a conducive environment for good crop production to match demand, helps keep prices in check, and strengthens rural demand.

[3] https://www.investindia.gov.in/sector/retail-e-commerce/food-retail
[4] "Digital SMBs," Zinnov
[5] India Brand Equity Foundation; Telecom Regulatory Authority of India
[6] "The Indian unicorn landscape," Invest India, September 7, 2022.
[7] ONDC Report, GoI

The government could continue focusing on the rural housing scheme or allocating a good amount towards improving rural infrastructure to drive consumption.

Expectation#3: Employment framework

(i) Define regulatory framework for the last mile delivery workforce

Industries such as e-commerce, food tech, logistics, and retail are set to increase recruitment of temporary staff, mainly in delivery, logistics, warehousing, sorting, and packing positions. However, gig workers encounter issues such as income instability, unpredictable hours, and the absence of crucial benefits, such as health insurance, retirement plans, and paid leave.

The number of gig workers has seen a continuous increase in metro and tier-1 markets wherever the e-commerce and hyper-local deliveries have expanded. Governments need to make efforts to acknowledge gig workforce as formal workforce under labour laws.[8]

Gig workforce needs to be regulated in India, as over a million people are expected to join this workforce in the next decade. Failure to promptly establish a regulatory framework for gig workers will adversely affect the burgeoning digital economy and its workforce. The government should initiate tripartite consultations to comprehend the intricacies of the gig economy and craft a balanced legal framework that harmonises business growth with the welfare of gig workers.[9]

(ii) Increase scope of employment generation incentives

- The threshold limit of emoluments of employees should be increased to INR 50,000, to widen the ambit of section 80JJAA.
- The available deduction of 30 percent may be increased to 50 percent to incentivise the industry to generate more employment avenues.
- The time period for claiming deduction may be increased from 3 years to 5 years. This will ensure that newly incorporated companies are able to avail the benefit of this provision. It may be noted that, companies may incur losses in the initial years of operations. Hence, they may not be able to claim such deduction.

Expectation#4: Tax and regulatory framework

(i) Ensure stability by fostering a fluid regulatory environment

In a dynamic retail sector where retailers operate at various scales, the ability to adapt to changes in regulations varies significantly. To ensure timely exchange of critical information and regulatory directives, establishing a flexible and informative mechanism is imperative. For instance, in fiscal year 2023 alone, more than 5,000 regulatory updates were disseminated through the union, state, and local government websites, typically in the form of notifications, gazettes, and circulars. These updates often lead to modifications in forms, deadlines, frequencies, penalties, and other aspects. Most of these alterations come into effect almost immediately, demanding swift interpretation and implementation. Hence, considering a compliance system accounting for the scale and risk profile of each retailer in the sector, is essential.

(ii) Clarify the perquisite valuation rules for electric vehicle

- The Government of India encourages manufacture and use of electric vehicles to promote sustainability. Many corporates provide car facility to their employees through leasing. The perquisite value of these benefits is determined per Rule 3 of the Income tax Rule, 1962. According to the Rules, valuation is based on the cubic capacity of the engine.
- Electric cars have motor instead of engine and battery capacity is measured in Kilowatts (kW) instead of cubic capacity. In the absence of specific clarification, corporates offers only petrol/diesel cars to its employees.

(iii) Resolution of undue hardship on e-commerce operators for TCS compliance on facilitation of sale of air ticket

- Every e-commerce operator is required to collect an amount calculated at rate not exceeding 1 percent of the net value of taxable supplies made through the operator, by other suppliers, where the consideration with respect to such supplies is to be collected by the operator.

[8] https://indianexpress.com/article/cities/pune/ola-uber-food-delivery-workers-strike-draw-attention-plight-8992623/
[9] https://www.deccanherald.com/opinion/gig-workers-merit-a-better-deal-1209798.html

- As an industry practice, in case of sale of airline tickets, an e-commerce operator deposits Tax Collected at Source (TCS) on its own and later recovers that from the airline. This leads to blocking of funds for an e-commerce operator for a considerable time. Thus, compliance with TCS provisions vis-à-vis airlines is causing great economic hardship to online travel agents who are committed to ensure full compliance with GST laws.
- The intention of TCS provisions was to avoid tax evasion by suppliers listed on the ECO platform. As the aviation industry is the most organised sector and regulated by IATA, provisions of TCS should be amended to exclude taxable supplies by an airline.

(iv) Time to make the compensation cess "compensatory" for consumers

- On implementation of the much-awaited GST law in 2017, the government decided to compensate states for the loss of revenue, by imposing a levy known as "compensation cess". While the levy was meant for the first five years from the introduction of GST, it has now been extended until 2026.
- Coupled with the burden in terms of longevity, the rise in rates of levy for MUVs and luxury sedans has made the segment unaffordable for most consumers. Higher rates will not only directly affect consumers but will also have indirect consequences in terms of increased pricing for taxis, higher logistics burden, etc. To address the limited volume growth of the industry, the government may reconsider high rates.
- Additionally, restructuring the import duty scenario for the said segment and EVs, may bring relief to the industry and promote green mobility. Slashing import rates for EVs should be the government's top priority as it will boost the automotive sector and support the logistics and transportation sector.

(v) Relief in the form of clarifications and relaxations - Placement of equipment at customer location for utility

- Several companies place their equipment at the location of their customers, with a pre-requisite that such customers will regularly procure minimum quantity of consumables from companies.
- There is a deliberation amongst stakeholders on whether this minimum purchase obligation serves as a consideration for placement of equipment and whether it should be taxed as leasing of equipment. Inter alia a clarification shall be issued in this regard, to throw light on the taxability of such transactions.

(vi) Clarify the ambit of taxation of benefits, perquisites

- The terms "benefit and perquisite" under section 194R may be defined to provide certainty regarding taxable transactions. Moreover, separate rules for valuation may be provided (similar to valuation of perquisites provided by an employer to employee).
- It may be clarified that in case of multi-level distribution channels, withholding tax provisions are required to be applied only at one level (say, by the manufacturer). This will avoid double taxation of the same amount.
- It may also be specified that withholding is required to be done in the hands of the actual recipient only and not in case of pass-through arrangements. For instance, manufacturers may provide benefit or perquisite to retailers through distributors. At present, manufacturers withhold taxes under section 194R while providing the benefit to the distributor, who also withholds taxes while passing onward to retailer (intended recipient).
- It may also be clarified that brand-building items, such as, billboards, standees, and stationery, with company logo/ name placed at prominent places in dealer premises, are not tantamount to any benefit. These are advertisement expenses incurred by the taxpayer and appropriate withholding may be done while purchasing the said materials.

(vii) Rationalise withholding tax provisions applicable to e-commerce operators

- In case multiple e-commerce operators are involved in a transaction, withholding tax under section 194-O may be applied only on incremental amounts vis-à-vis different components/legs of the supply chain (say, distributors, retailers, etc.), instead of the gross amount, to avoid cascading effect.
- Further, the mechanism contemplated in section 194-O of the Act does not consider two platforms. In situations where clicks on specific tabs of one vendor directs customers to another vender, it may be clarified that the website of first vendor is not facilitating the transaction for second vendor by merely hosting the option to avail goods/services from another vendor.
- The threshold may be increased to INR 40 lakh (at least for individuals and HUFs) to align with the threshold for GST registration prevalent in most states.

- It may also be clarified that TDS should be applied on the amount in excess of the minimum threshold, similar to section 194Q.
- It may be clarified that sales returns or cancellations and charges incidental to sale of goods or services shall be excluded while computing “gross amount.” TDS may be applied on the net amount of sales similar to GST. This will align TDS and GST provisions.
- Exemption may be provided in case the sale of goods or services is facilitated to a non-resident customer, similar to section 206C(1H) relating to TCS on sale of goods.
- It may be specifically clarified that the provisions are not applicable on non-resident e-commerce operators.

(viii) Tax deduction at source on purchase of goods under section 194Q and TCS on sale of goods

- At present, the provisions of section 206C(1H) require the seller to collect TCS at 0.1 percent from a buyer on sale of goods, subject to certain conditions. Further, the provisions of section 194Q requires the buyer to deduct TDS on purchase of goods at 0.1 percent before making payment to the seller, subject to certain conditions. Therefore, the same transaction is subject to both TDS and TCS.
- While the primary liability is on the buyer to deduct TDS, in case the buyer does not deduct TDS, the seller is required to collect TCS under section 206C(1H) and pay interest in case of delay in deduction and deposit of TCS under section 206C(1H).
- This causes undue hardship to the seller in case of failure by the buyer, as non-deduction of tax will be noticed by the seller only upon receipt of the consideration from the buyer. It also leads to revising TCS returns of earlier quarters and accounting challenges.
- In view of above, TDS should be applicable on purchase of goods. It should be the buyer’s responsibility to deduct TDS. Consequences of non-deduction should be on the buyer. In such cases, provisions of section 206C(1H) should not be made applicable to the seller.

Financial services and financial inclusion

Himanish Chaudhuri
Partner and Financial Services Leader

Current environment

- According to the International Monetary Fund,[1] while the world economy is expected to grow at no more than 3 percent, India is expected to see one of the strongest growth rates of 6.3 percent in 2024. India's growth will be driven by strong financial inclusion and consumer demand, a young demography, and improving trade balances. However, a slowing global economy, coupled with a divergent economic landscape, will challenge the financial services industry's ability to generate income and manage costs.
- Multiple disruptive forces, such as higher interest rates, decelerated spending, assertive regulations, climate changes, and conflicts/geopolitical tensions, will play a role in the sector's transformation.
- Innovative banking models focussed on payments and small finance banks, coupled with major reforms around digital payments, payment aggregators, neo-banking, rise of Indian NBFCs, and fintechs, will continue to significantly enhance India's financial inclusion and fuel the credit cycle.
- Over the past few years, financial inclusion initiatives have achieved a certain momentum in banking services penetration. The next step is to increase digital inclusivity. Banks provide digital services to enhance convenience to customers. Their digital transformation initiatives are expected to simplify processes and reduce cycle time to carry out transactions. However, changes in the processes may affect a large section of customers who are used to traditional banking methods.
- Although, RBI's efforts to combat inflation and tighten monetary policies are showing signs of success, there is still uncertainty due to the above-mentioned factors. This, coupled with the General Elections in 2024, could complicate the economic growth. However, India is poised for a brighter future. The government's priorities would be to achieve sustained disinflation while ensuring financial stability and inclusion, by remaining focused on restoring price stability, reducing inefficiencies, fostering competition, and strengthening financial supervision and risk monitoring.

Expectations

Top asks

- **Expectation #1 – Clear and concise Indian capital gains tax regime to boost capital markets**
  - India's capital gains tax regime has been perceived as complex, due to multiple rate slabs, differentiated outcomes linked to holding periods for different assets, including different financial securities and the same class of assets (short term vs long term), etc.

[1] IMF, World Economic Outlook Update, July 2023

- Predictability and certainty of capital gains regime is vital for investment decisions by most strategic and portfolio investors.
- A simplified structure for taxing capital gains on equity, debt hybrid, and other types of financial securities, will keep Indian capital markets vibrant and provide a more predictable returns framework for investors.
- To this effect, the following measures may be considered:
  - Reduce the total number of tax rates applicable to capital gains
  - Uniform rate of surcharge for classes of foreign investors and similar treatment for different type of investors
  - Rationalisation of holding period for different capital asset classes
  - Allowing fungibility of long-term and short-term capital losses

- **Expectation #2: Propel IFSC GIFT City activities**
  - IFSC–GIFT City has taken off well for the banking, asset management, aircraft leasing, insurance, and reinsurance sectors. It has also become an attractive destination for family offices and GICs. However, there are still some stumbling blocks due to uncertainties and short sightedness of term benefits.
  - For the IFSC-GIFT City to serve as a dedicated financial sector hub, giving competition to other international markets, the following measures may be considered:
    - Increasing the longevity of the income-tax deduction benefit, exemption from applicability of domestic transfer pricing requirements and GAAR to transactions with IFSC units, incentivising companies/individuals through fiscal incentives for enabling smooth movement of skilled personnel to IFSC-GIFT City.
    - The IFSCA has issued regulations to provide a framework to undertake Global/Regional Corporate Treasury Centres (GTC) activities by finance company/finance units in IFSC GIFT City. However, GTCs face challenges due to the following reasons:
      i. Applicability of deemed dividend provisions on loans/advances amongst group companies; this results in the taxing of the entire amount of loan/advance made to group companies, making it tax ineffective.
      ii. Applicability of withholding tax on payments made to/received by GTC, despite the income-tax holiday; this results in the blockage of working capital and/or increase compliance burden of obtaining refund/lower withholding tax certificate, etc.

      Therefore, a specific carve-out from applicability of deemed dividend provisions and withholding tax for entities in IFSC GIFT City may be considered.
    - To curtail migration of family offices to Singapore and Dubai, and enable onshoring of existing family offices to IFSC GIFT City, the Liberalised Remittance Scheme (LRS) limits may be increased for investments through IFSC GIFT City. Moreover, a suitable clarification on characterisation of Family investment Fund (FIF) investments as ODIs/OPI would boost such FIFs set-ups.

- **Expectation #3: Accelerating technology adoption**
  - The impact of generative AI, industry convergence, embedded finance, open data, digitisation of money, cloud computing, decarbonisation, and digital identity will likely grow in 2024. With this, the incidence of frauds will also increase.
  - Although Indian fintechs are leading technological transformation and ensuring a seamless cross-border payments systems, Indian banks and NBFCs would need to play a critical role in making India a world leader. Banks and NBFCs would need to keep pace with the constant technological advancements, warranting significant outlay in R&D, new technology adoption, building appropriate systems/interfaces, data migration, and fraud prevention.
  - Hence, to accelerate technological adoption and encourage digital innovation with adequate safeguards to counter fraud, ensure data privacy, avoid tax leakages, etc., regulatory and tax relaxations (such as weighted tax deductions on infrastructure cost, data warehouses, research expenditure, and training institutions) may be considered. Alternatively, advancing tax deductions through re-characterisation of capex expenditure as revenue expenditure, may be considered.

The following measures would also promote financial/digital inclusivity:

(i) Transitioning from financial inclusion to digital inclusivity

- Every financial service provider forms a "Digital Banking" committee on the lines of Policyholders Protection Committee (IRDAI) with the sole purpose of measuring and improving digital inclusivity of their new and existing customers.
- The regulatory oversight on such a committee will be by an advisory committee under the Ministry of Finance. This will be a committee common to apex regulators, to integrate their digital policies and offerings in a way that service providers do not have to run multiple governance and oversight initiatives for each apex regulator.
- A separate sub-committee will work on arresting digital fraud and protecting customers new to digital adoption.

(ii) Unifying the KYC authentication process

- Banking account holders have products with one or more of the apex regulators. These products include insurance, mutual fund, securities, and pension. A consistent or unified KYC authentication process will enhance customer convenience significantly without duplicating efforts across stages of transaction lifecycle – from account opening to death and transmission. To fulfil this objective, the current KYC process may be refined, and the UIDAI infrastructure is enhanced under the overall policy guidance of RBI.

Policy recommendations and expected impact

- To promote the start-up and infra spaces, the following policy measures may be considered:
  - Introduction of a simple and specific tax and regulatory framework, for PEs, VCs, and start-ups
  - Extension of the qualifying investment time limit for SWFs/FPFs from 2024 to 2030, the time when India is expected to become the third-largest economy.
  - Extension of the tax benefits granted to SWFs and FPFs to other regulated patient capital investors, subject to suitable safeguards, minimum quantum, and agreed lock-in conditions.
- Financial services players need to play an important role in combating climate changes. Therefore, incentivising investment in green bonds and renewable energy business would help India achieve net zero emission targets by 2070 and meet 50 percent of energy requirements from renewable energy sources by 2030.
- To promote long-term savings through National Pension System (NPS) and reduce the tax burden for senior citizens above 75 years, the annuity portion of the NPS should be made tax free for NPS holders from the age of 75 (they will continue to bear the tax until the age of 60 to 75). Moreover, NPS can be included, along with interest and pension, to ensure that senior citizens above 75 years of age do not have to file returns if they have NPS proceeds. At present, the lump-sum withdrawal of 60 percent is tax-free.

Life sciences & healthcare

Joydeep Ghosh
Partner, Industry Leader
Life Science & Healthcare

Current environment

- The Indian pharmaceutical industry commands a significant share of more than 20 percent in the global medical supply chain. While India ranks third globally in terms of production volume, the industry ranks 10th globally in terms of value addition. This highlights the need for improved local value addition capabilities that can be addressed through appropriate policy interventions.
- The government of India has been constantly taking several measures to encourage investments in the sector and promote local manufacturing and consumption, keeping cure and prevention in perspective. Production-linked incentive schemes have been introduced for medical devices, pharmaceuticals, and bulk drugs. The government has also introduced schemes to promote medical device parks and bulk drug parks with financial grants across different Indian states. Initiatives such as Ayushmaan Bharat Digital Mission ("ADBDM"), CoWIN (a digital vaccine delivery platform), health registry, and telemedicine, highlight the government's strong emphasis on digitisation of health in India. Further, introduction of the Scheme for Promotion of R&D and Innovation in Pharma Med Tech Sector (PRIP) in September 2023 showcases the focus on creating an ecosystem for innovation and research. The industry is expected to witness an accelerated growth in the future led by various factors, such as policy interventions, infrastructure development, Foreign Direct Investments (FDI), improved manufacturing capabilities, and access to the cost-effective talent pool.

Expectations

Healthcare delivery: Enhancing the overall healthcare system in the country

In the past few years, the healthcare sector has been a priority for the government, with a steady increase in allocations in previous budgets. In the Union Budget 2022-23, the Ministry of Health and Family Welfare received an allocation of about INR 86,200 crore, representing a 16.5 percent increase compared with the previous year. However, to increase the penetration of digital health, the following things can be done:

- Awareness campaigns for diseases and the patient care availability nearby
- Consolidation of data – health records, past medical records, etc. – improved chronic disease management, promote medication, and treatment adherence
- Training for nurses, midwives, and semi-professional support staff on telemedicine
- Emergency care through satellite kiosks and medicines through drone facility

Direct Tax

- **Expectation #1: Extension of sunset date for qualifying for concessional tax rate on income of new manufacturing domestic companies**
  - The Taxation Laws (Amendment) Act, 2019, inter-alia, inserted section 115BAB to Act provides that new manufacturing domestic companies set up on or after 1 October 2019 commence manufacturing or production by 31 March 2023. These companies do not avail of any specified incentive or deductions; they may opt to pay tax at a concessional rate of 15 percent.

- The time for commencing manufacturing or production was extended to 31 March 2024 by the Finance Act, 2022.
- Considering that the government promotes companies to "Make in India", we request that the time limit for commencing manufacturing or production be further extended to 31 March 2026.

- **Expectation #2: Modification of sub-section(2)(b) of section 115BAB**
  - Section 115BAB provides a concessional tax rate of 15 percent to the company that is engaged in the business of manufacturing or production of any article or thing and research in relation to, or distribution of, such article or thing manufactured or produced by it.
  - Considering that the government intends to promote research, innovation, and development in India, we request that companies involved only in research-related activities should be included for concessional tax rate under section 115BAB. The concessional rate should not be restricted to only research in relation to article/thing manufactured or produced by the company.
- **Expectation #3: Extension of the sunset clause for Section 194LC**
  - For interest income on borrowings in foreign currency up to 1 July 2023, the concessional tax rate is 5 percent. This has significantly provided a viable and attractive avenue for raising funds by Indian businesses, thus helping India to maintain the momentum in economic growth over the years.
  - Therefore, the sunset period should be extended for borrowings in foreign currency up to 31 March 2026; this would support the vision of "Make in India".
- **Expectation #4 Clarification on product samples and low brand value items**
  - According to CBDT circular no. 18 of 2022 (Question No. 4), section 194R is applicable on free samples.
  - Given that the Drugs and Cosmetics Rules of 1945 acknowledge the practice of supplying drugs as free samples to medical professionals, it is advisable to consider the distribution of free product samples up to a permissible limit as a legitimate marketing expense. This should be eligible for deduction under section 37 and should not be subject to the provisions of section 194R.
  - As MCI regulations do not provide penalty for accepting gifts of value below INR 1,000, low-value brand reminders up to INR 1,000 per item given as part of marketing activity should be allowed as deduction under section 37.
- **Expectation #5 Re-introduction of weighted deduction under section 35(2AB)**
  - For a company engaged in the business of bio-technology or in any business of manufacture or production of any article or thing, not being an article or thing, weighted deduction of 200 percent up to March 2017 and 150 percent up to March 2020 was allowed on the expenditure incurred on scientific research (not being expenditure in the nature of cost of any land or building) on in-house research and development facility as approved by the DSIR.
  - To promote research, innovation, and development in India, weighted deduction for expenditure on R&D should be reintroduced.

  Further, eligibility to weighted deduction should be extended to companies that have opted for the new tax regime. The new regime entitles a lower tax rate of 25.17 percent as a majority of the companies are covered by this tax rate.

Indirect Tax

- **Expectation #1: Eligibility of Input Tax Credit ("ITC") availed by the pharmaceutical companies on payments made to medical practitioners**
  - The Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002 ("MCI Regulations") prohibit medical practitioners from accepting payments from pharmaceutical and allied health sector industries. There has been an amendment under income tax provisions to disallow such expenses incurred by pharmaceutical companies in violation of MCI regulations.
  - The amendments in the MCI regulations, along with the recent corresponding changes in the Income tax provisions, have also affected the eligibility of ITC availed by pharmaceutical companies on such payments made to medical practitioners.
  - The GST authorities plan to issue summons to pharma companies alleging that as expenses are disallowed as a business expenditure under the Income Tax law, the same is construed to be used for non-business purpose.

Hence, ITC should not be allowed under the GST provisions, even though the GST law does not impose any such restrictions.

- The government issues clarifications, thereby allowing ITC on such eligible business expenditure incurred on medical practitioners. These clarifications are essential for the industry at large and help alleviate unnecessary litigations and uncertainties.

- **Expectation #2: Bring GST rate on APIs at par with the formulations**
  - At present, APIs attract a higher GST rate of 18 percent vis-à-vis formulations that attract a lower rate (12 percent/5 percent), leading to accumulation of credit for the pharma industry. Significant expenses on capital goods also add to credit accumulation.
  - Although GST law provides for refund of accumulated ITC to address this issue, possibilities of inordinate delay cannot be ruled out.
  - The government should align the GST rate for APIs with a lower rate for pharma formulations. In other words, the GST rate across the supply chain for the pharma industry should be at the lower rate of 12 percent to effectively address the issue of credit accumulation, impact on working capital, and inordinate delays in obtaining refund.

- **Expectation #3: ITC reversal on physician samples and expired good**
  - GST law provides that ITC on goods lost, stolen, destroyed, written off or disposed of by way of gifts or free samples is required to be reversed. A literal interpretation of this provision in the pharma industry leads to adverse consequences, such as in cases of physician samples.
  - Making samples available to physicians is a time-tested and established industry practice. Therefore, such transactions should not fall within the ambit of the restriction.
  - The similar issue is faced with mandatory destruction of expired drugs/medicines. As this is a statutory requirement, this should not entail any adverse GST consequences in the form reversal of ITC.
  - The government may address these issues on priority, providing long-awaited relief to the pharmaceutical industry.

- **Expectation #4: Clarification on GST payable under Reverse Charge Mechanism ("RCM") for payments to foreign group entities for seconded expat employees to Indian entities**
  - The Supreme Court of India, in case of Northern Operating Systems Pvt. Ltd., has ruled that tax is applicable under RCM for payments made to foreign group entities concerning seconded employees to Indian entities.
  - Following this judgment, numerous pharmaceutical companies have been receiving notices from GST authorities, requesting details of such transactions, and subsequently issuing demand notices for the tax and interest amounts. Additionally, authorities are alleging Input Tax Credit (ITC) claims, which is significantly affecting working capital of these companies and increasing their operational costs.
  - Given the intricate nature of this issue and the substantial financial burden faced by companies due to interest payments and ITC disputes, the government should consider issuing a notification and circular to clarify the applicability of GST, interest, and the eligibility of ITC. Such clarifications would provide the much-needed relief to the industry.

Regulatory

- **Expectation #1: Streamline the existing regulatory framework through “one regulator” approach**
  - Multiple regulators regulate multiple licences and compliances for both pharmaceuticals and medical devices. For instance, drug licence is required for each state, separately for each category. The central licence is also required for clinical trials and new drug approvals. Similarly, in case of certain category of drugs/medical treatments, additional approvals from PESO, Atomic Energy Regulatory Board, may be required. For pharma and medical devices policies, the Department of Pharmaceutical is the nodal agency.
  - Due to the multiplicity of regulatory processes and multiple regulators, undertaking operations become complex and time consuming. In addition, the practice adopted by different regulators for licensing and enforcement varies in each state.
  - In light of the above, the government should consider forming a single regulatory authority each for pharmaceuticals and medical devices with experts from across the sectors on board.

- **Expectation #2: Offer additional incentives to promote manufacturing of pharmaceutical products, including research in India**
  - Providing tax incentives through additional deductions under Income Tax Act (as was earlier provided under Section 35(2AB)) and GST exemptions for companies participating in PRIP can serve as a powerful catalyst for advancing investments in innovation and product development. This has been implemented globally, including China.

  Providing preference of procurement in the government tenders for Indian manufactured products especially where R&D is performed in India for developing such products.

  - To encourage greater participation by foreign companies in the public procurement process (Public Procurement (Make in India) Order 2017) and promote increased local value addition/ manufacturing in India, the government should consider providing preferential treatment to the companies participating in the PRIP scheme and Production Linked Incentive (PLI) scheme. In addition, the concept of offsets should be introduced while computing the local content. Hence, value addition should be considered on a composite basis.
  - This concept would encourage companies to proactively participate in PRIP and PLI with a longer-term vision of enhanced market access. This would also provide a much-needed push to the government's Make in India vision of becoming a global manufacturing hub.

- **Expectation #3: Incentivise companies to undertake skill development initiatives for pharma/healthcare professionals**
  - Indian head-quartered pharmaceutical manufacturers strongly feel the need for regular hands-on upskilling of people working or entering the pharma sector in operations' roles, particularly in the manufacturing and quality functions. To incentivise organisations for providing funding to such training institutes, the government can propose an additional deduction (1.25 times) on the funds spent by organisations for this purpose.
  - A recent WHO report estimated a shortage of about 1.8 million health workforces in India and suggests that to meet the threshold of 34.5 skilled health workers per 10,000 population, there will be a shortfall of 0.16 million doctors and 0.65 million nurses/midwives in the total stock by 2030.
  - This emphasizes the need to scale-up high quality, transformative education, and reinforce skill development as a major focus area to meet the increasing demand. To achieve this, strong collaboration should be fostered between skill training institutions and the industry to align training with the current and future needs of the job market.
  - For the same, the government should consider providing incentives to the industry for undertaking skill development initiatives for paramedics in government hospitals and colleges/ universities. The incentives could in the form of:
    - financial incentives and cash subsidies
    - formal certification for skill development programmes, such as accreditation by Medical Council of India (MCI), to enhance credibility and recognition amongst employers
    - apprenticeship opportunities to ensure ready resource availability for employers
    - cost-sharing of training programmes by National Skill Development Corporation (NSDC)
    - targeted skill development initiatives for women and marginalised groups to help the industry meet inclusivity targets

- **Expectation #4: Expansion of the coverage of insurance to modern treatment methods notified by IRDAI**
  - The Ayushman Bharat-Pradhan Mantri Jan Arogya Yojana (PMJAY) provides health insurance coverage for the citizens and covers a vast list of diseases and treatments. However, the PMJAY does not cover the defined list of modern treatment methods and advancement of technologies.
  - IRDAI has included the health insurance coverage for 12 such modern treatment methods under Chapter V of the Guidelines on "Standardisation of exclusions in health insurance contracts".
  - With these modern treatment methods and advancement of technologies now being used more frequently by hospitals, covering them under the AB-PMJAY insurance can help economically weaker sections access better healthcare. This will also expand the scope for private health insurance companies to include them in their products, irrespective of the package cost.
  - This can ensure equitable access to modern treatments for public in line with global healthcare standards.

Global capability centres

Gaurav Gupta
Partner and GCC
Industry Leader

Current environment

- The India GCC journey continues to see growth with more than 1580 GCCs currently in India employing 1.66 million people. The matured technology ecosystem, talent, and cost advantage, politically stable environment amidst global uncertainty are the main factors for India being a successful GCC global leader and a preferred location for set up.
- In the next two years, GCCs has a potential to move up to 1900 centres in India, employing 2 million people with a revenue of US$60-80 billion. However, to realise the full potential, GCCs would need support in infrastructure development, increased investment in skill development, consistent taxation policies, and an ecosystem fostering innovation.
- GCCs continue to invest in hiring and upskilling talent and developing skills across the board including in niche areas. They also focus on developing leadership roles within and from GCCs as we see a rise in global roles being anchored from GCCs.
- The current direct tax policy landscape in India is constantly evolving, driven by the government's efforts to reform existing systems and processes, with a focus on improving efficiency and transparency.
- Significant measures, such as the reduction in corporate tax rates, the introduction of concessional tax regimes, and the elimination of the minimum alternate tax regime, have been undertaken to attract investment and foster a favourable business-friendly tax climate. The Indian government has also adopted various globally accepted best practices to provide trust and confidence to foreign investors and prevent disputes. Safe harbour rules, Advance pricing regime, effective MAP programme, and adoption of sixth method for transfer pricing analysis are a few examples.
- The pool of digital talent in India with expertise in areas of cloud computing, Artificial Intelligence (AI), big data, and Internet of things (IoT) grew at a CAGR of more than 35 percent over the past four years. The talent pool is expected to reach 2.6 million by 2024. Due to higher availability of digital skill and capabilities in India, we see a rise in the number of GCCs in India, driving digital transformation initiatives for their parent organisations or having a significant involvement in them.
- The use of data analytics and advanced detection tools has helped the government detect and prevent delinquency in relation to input tax credit and facilitate free flow of input tax credit.
- In its journey of enhancing ease of doing business initiative, the government had taken up the task of consolidating various labour regulations into Four Labour Codes. This will meet the business objectives of simplification of varied statutes to companies in compliance, minimisation of litigation, and realignment to reflect current business requirements. Personal taxation shows a buoyant growth across different income groups bundled with tax-payer friendly and tax-payer oriented progressive policies, such as implementation of the new tax regime.

Expectations

Top asks

- **Expectation #1: Enhance export incentives for GCCs**

  Measures towards expansion of export incentives (such as section 10AA of the IT Act, now defunct) can contribute to the growth and success of GCCs in India, while maintaining India's key position as a preferred global hub for business operations. Further, set-up and operation of new GCCs could be extended a benefit of reduced corporate tax regime of 15 percent similar to new manufacturing domestic companies.

- **Expectation #2: Developing tier 2 locations to become mature GCC hubs**

  Bengaluru, Hyderabad, Delhi, Chennai, Mumbai, and Pune are the prime GCC locations and are considered mature hubs for GCC set-ups.

  However, recently, there has been a slowdown in the growth of these matured hubs due to multiple factors. With remote work, the opportunity for GCC talent to work outside these locations became a reality. At the same time, the pressure on the infrastructure of these locations continues to be a challenge. The costs of talent and operations are also increasing. Consequently, companies are exploring alternative locations to set up or expand their operations outside India.

  Hence, we should look at developing our tier 2 locations, such as Ahmedabad, Kolkata, Coimbatore, and Indore, to attract companies to open/expand their centres in these locations. The government should work on developing advanced infrastructure and provide a supportive business environment to GCCs in Tier 2 locations. The government should also invest heavily in education and training programmes to ensure that the talent in these locations is well-equipped to meet the demands of the niche skills required in GCCs.

- **Expectation #3: Extend the advantages provided to International Financial Service Centre (IFSC) in GIFT City to sectors beyond the financial services industry**

  With its special economic zone status and various incentives, GIFT City has become an attractive destination for foreign companies, but the tax benefits for IFSCs (in GIFT city) are currently limited to the financial sector. Broadening these tax benefits to other sectors is essential to unlock the full potential of GIFT City as a hub for GCCs and promote economic growth. To realise these benefits, tax benefits and regulatory incentives of GIFT City should be extended to each sector in which GCCs operate.

- **Expectation #4: Encourage innovation, support start-up ecosystem, and promote R&D through weighted deductions**

  In today's age, GCCs are transforming into globally integrated innovation-focused strategic hubs by driving innovation through internal initiatives and collaborating with external ecosystem. Innovation has become a key focus area for GCCs. The government can look at setting up incubation hubs for innovation and provide incentives to GCCs that innovate and generate intellectual properties in India. Given that start-ups are at the leading edge of innovation, the government should look at creating an ecosystem to encourage start-ups to innovate and generate more intellectual properties and licences. The government should encourage technological innovation and promote competition through increased incentives and tax concessions for R&D and attract industry players to invest in more innovation and R&D.

  The government may consider restoring weighted deductions for R&D expenditure and donations to scientific research institutions that were available in the past. By reinstating these tax incentives, India can further foster innovation and position itself as a hub for cutting-edge R&D activities especially for GCCs.

- **Expectation #5: Investing in advance skill development**

  As GCCs are moving up the value chain, they are now driving innovation, digital, and technology transformation initiatives. More than 50 percent of India-based GCCs plan to invest in emerging technologies. For example, in the past few years, over 30 new centres for R&D and more than 60 centres for digital work have been set-up in India. To support growth in these new areas, GCCs require skills in areas such as Gen AI, Artificial Intelligence, Machine Learning, Robotic Process Automation, Machine Learning, Analytics, and Cloud. In future, the demand for these skills will only increase and India's ability to attract GCCs will depend on availability of these advanced skills. Hence, the government should look at supporting stakeholders to open more institutions and labs that offer training courses in these areas and encourage current institutions to keep innovating their curriculum with active industry participation from GCCs. The government should also consider large-scale industry internship programmes and incentivise GCCs to invest in skill development (such as the incentive on capital expenditure in manufacturing).

- **Expectation #6: Revision of safe harbour rules to reduce litigation**

  The government may re-evaluate the safe harbour provisions on three aspects: (1) reduce the class of transactions from the safe harbour and restrict it only for IT, ITeS, business support, etc.; (2) increase the coverage of transactions (such as marketing support, and distribution); (3) provide the safe harbour rates closer to comparable benchmarks with a little premium for certainty; and (4) increase the threshold to cover almost 75 percent of the companies under this spectrum. This can serve dual purpose of providing tax certainty to taxpayers and easing the burden of the APA.

- **Expectation #7: Infrastructure development and sectoral policy interventions by state governments of mature GCC hubs**

  Most GCCs in India are present in Bengaluru, Mumbai, NCR, Hyderabad, Pune, and Chennai. However, these big cities are reaching saturation with infrastructure not able to keep up pace. There is a need for infrastructure development in these cities. The government should look at increasing physical and digital infrastructure investment and incentivising organisations and state governments to proactively build GCC parks/hubs and infrastructure that can be used for the GCC set-up. This will attract more GCCs and reduce set-up time that currently runs from 3-9 months for space identification, approvals, physical set-up, etc.

- **Expectation #8: Allowance of GST credit on capital goods and immovable property, and removal of credit restrictions on employee-related expenses**

  Key requirements for GCCs include the allowance of GST credits paid on capital goods and credits related to immovable property. Additionally, the removal of credit restrictions on employee-related expenses remains a subject of ongoing representations to the government. Allowing credits on such expenses would help ease working capital commitments of captive GCCs and align with the government's objective to export taxes.

- **Expectation #9: Bengaluru to be considered a metro city for the purpose of 10(13A)**

  The Constitution of India recognises Bengaluru as a metro city amongst other cities such as NCR, Mumbai, Kolkata, Pune, Hyderabad, and Chennai. Bengaluru is ranked as one of world's fastest-growing cities and has provided employment opportunities to many. However, there is raise in the cost of living in the city compared with other cities. Hence, employees should get the benefit of a 50 percent deduction for HRA.

Taxation

Direct taxation

Rohinton Sidhwa
Partner

Current direct tax policy landscape

- India is poised for significant economic expansion backed by a politically stable environment amidst global uncertainty. This is particularly evident as international investors actively seek to diversify and reconfigure their supply chains.
- The current direct tax policy landscape in India is constantly evolving. It is driven by the government's efforts to reform existing systems and processes, with a focus on improving efficiency and transparency.
- Significant measures, such as reduction in corporate tax rates, introduction of concessional tax regimes, and elimination of the minimum alternate tax regime, have been undertaken to attract investment and foster a favourable business-friendly tax climate.
- The government has started implementing measures involving automation using technology to enhance transparency and efficiency in tax administration.
- While policymakers continue to focus on harmonising tax rates, incentives to attract investment, the tax policy landscape remains complex and challenging due to the impact of various judicial decisions and legislative amendments..
- Despite these challenges, the current tax environment in India presents significant opportunities for a more taxpayer-friendly and investment-attractive system.

The tax policy administration can undertake the following measures to use this opportunity.

Expectations

Top asks

Expectation #1: Extending concessional corporate tax rate for new manufacturing companies

- The existing concessional corporate tax rate, set at 15 percent, has been pivotal in attracting investments into India. This rate is currently available to new domestic manufacturing companies under Section 115BAB. However, a crucial requirement for these companies is to commence manufacturing operations by 31 March 2024.
- Introduced in 2019, this concessional rate yielded remarkable results, significantly boosting the influx of Foreign Direct Investment (FDI) into the Indian manufacturing sector. To put it in perspective, there was a substantial increase in FDI, from INR 89,766 crore in FY 2020-21 to an impressive INR 1,58,332 crore in FY 2021-22, showcasing a 76 percent surge (source: https://pib.gov.in/PressReleasePage.aspx?PRID=1846088).
- Recognising the substantial role this measure has played in advancing economic objectives and attracting foreign investments, the tax policy administration may extend the sunset clause of this regime for an additional two years. This extension will undoubtedly contribute to India's economic growth, enhancing the country's attractiveness to investors.

- The new import policy that encourages domestic manufacture of Personal Digital Assistants (PDAs) and restricts import through its licensing model, has led to tech giants announcing plans for expansion of investment and manufacturing in India. These opportunities can be capitalised further.
- Extending the concessional tax rate would provide an opportunity for such investors who are currently in the process of setting up or considering India as a potential investment destination, to use this opportunity.

Expectation #2: Settlement scheme to resolve past tax disputes arising from differential treaty interpretations

- Foreign investors have often faced tax disputes arising from differences in treaty interpretation. Adding to this uncertainty is the recent decision by the Supreme Court in case of Nestle SA. The decision had wide ramifications on treaty interpretation and various treaty benefits that taxpayers have historically availed. A key takeaway from this ruling is the necessity for specific notifications from the tax policy administration under the Act, to implement treaty protocols, especially in the context of the "Most Favoured Nation" (MFN) clause.
- The tax policy administration will soon release specific guidelines regarding the interpretation of protocols to treaties between India and various countries. These guidelines will be intended for implementation in future transactions, promoting clarity and consistency in treaty interpretation.
- However, recognising the need to provide certainty and resolution for present cases where lower rate has already been claimed, the tax policy administration should consider establishing guidelines under a settlement scheme. Such schemes could provide one-time window for taxpayers to make voluntary tax payments of differential taxes, without interest or penalty. This initiative would offer relief and certainty to taxpayers, while also facilitating efficient collection of taxes from the perspective of the tax administration.

Expectation #3: Incentivising exports through the tax holiday regime

- The tax policy administration previously granted income tax exemptions to Indian companies engaged in exporting services, leading to substantial growth in the services sector. However, these income tax exemptions are no longer available due to the sunset provision under section 10 and section 80 of the Income Tax laws.
- Reintroducing a tax holiday or exemption could stimulate exports. This approach would attract foreign exchange and align with the government's "Make in India" campaign, encouraging Multinational Corporations (MNCs) to establish export hubs in India.
- To foster exports, the tax policy administration may consider reinstating tax exemptions for income generated from export of both goods and services. This would revitalise India's export sector and strengthen its position in the global market.

Expectation #4: Promoting R&D through weighted deductions

- Given the focus on promoting manufacturing, investing in R&D is crucial to facilitate development of advanced manufacturing processes and technologies. These advancements can spur innovation and strengthen the manufacturing sector's capabilities.
- Substantial investment in R&D, both in strengthening existing institutions and establishing new research institutions, is essential to reduce reliance on foreign technology and innovations.
- The government has introduced several policy initiatives, such as Atal Innovation Mission, and R&D policy in the pharma sector, to encourage R&D. Introduction of tax incentives, coupled with these policy measures, can effectively support the broader objective of the Make in India campaign.
- The government may consider restoring weighted deductions for R&D expenditure and donations to scientific research institutions that were available in the past. By reinstating these tax incentives, India can further foster innovation and position itself as a hub for R&D activities especially for Global Capability Centres.

Policy recommendations and expected impact

Recommendation #1: Facilitating corporate restructuring through enhanced tax provisions

- Companies encounter complexities during corporate restructuring, such as migration of tax credits, losses, benefits, and registrations due to the absence of a comprehensive mechanism/procedure/guideline under the income tax provisions in relation to corporate restructuring.

- To enhance corporate restructuring and minimise litigation faced by taxpayers during restructuring, comprehensive guidelines may be established covering various administrative aspects in relation to corporate restructuring, while also avoiding revenue leakage.
- These guidelines may be benchmarked against international best practices in corporate restructuring, ensuring alignment with global standards and promoting India as a favourable destination for corporate restructuring activities.

Recommendation #2: Reducing tax litigation through policy framework

- In the past, various government initiatives, including amnesty schemes and higher threshold limits for filing appeals, effectively reduced case pendency at tax tribunals, high courts, and the Supreme Court.
- After the implementation of the faceless appeal scheme, case pendency at the first appellate stage "CIT(A)" has surged, as recognised in the Finance Act of 2023. Notably, there are no prescribed timelines for disposal of appeals at this stage. Even during the introduction of the Vivaad se Vishwas scheme in 2020, more than 500,000 cases were pending at various fora. Despite the introduction of the Joint Commissioner (Appeals) last year to reduce this bottleneck and clear small disputes, there has been less impact on the majority of the pending appeals.
- While time limits exist for filing appeals at various fora, substantial delays were seen in revenue's appeal filings, as highlighted by a recent case with a 274-day delay in filing a Special Leave Petition (SLP) before the Supreme Court.
- Prolonged litigation without closure certainty results in significant time and effort for taxpayers and the tax administration.
- The tax administration may introduce timelines for appeals' disposal at the first appellate authority stage, akin to timelines established for the dispute resolution panel in managing objections filed by taxpayers.
- To expedite the litigation process and provide certainty, the tax administration may establish a comprehensive policy framework for appeals at higher fora (Tribunal, High Court, and Supreme Court). This framework should include designated authorities responsible for timely filing and diligent prosecution of appeals.

Recommendation #3: Addressing uncertainties on buyback taxation and providing clarity to foreign investors

- Buyback has been a commonly adopted exit/repatriation strategy for foreign investors. However, the taxation of cross-border buyback taxation has been a contentious issue in India. A recent ruling by a tribunal involving a global tech giant has further added to the ambiguity surrounding the applicability of dividend tax to buybacks.
- Given the current emphasis on attracting foreign investment, bringing clarity to the taxation of buybacks, is crucial. This would help alleviate uncertainties, minimise unnecessary litigation, and provide investors transparency on treatment of repatriation.
- The government may consider implementing specific regulations to address the taxation of different buyback scenarios. Taking cues from jurisdictions such as the US and the Netherlands (which have clear guidelines on the treatment of buybacks and applicability of dividend tax in such situations) would provide much-needed clarity for investors.

Recommendation #4: Rationalising litigation relating to charitable trusts

- Despite their complete income tax exemption, charitable trusts often generate incidental income from activities aligned with their charitable purposes. This has been a subject of past litigation, from registration procedures to fund application.
- The tax policy administration may consider introducing a concessional tax approach for charitable trusts as an alternative to full tax exemption. Charitable trusts could opt for this regime, benefitting from lower tax rates compared with standard income tax rates.
- This new regime should aim to simplify compliance requirements for charitable trusts, reducing the administrative burden associated with tax filings and documentation. This streamlining can enhance revenue collection without incurring litigation costs.
- The guidelines may also cover specific aspects for income treatment, accommodating both accrual and receipt bases. Charitable institutions should have the flexibility to choose the basis that aligns with their operational needs and objectives, ensuring a more tailored approach to their taxation.

Indirect tax - customs

Mahesh Jaising
Partner

Current environment

- The government shall present an interim Budget in February 2024. The Government's focus shall be on Make in India, creating job opportunities, and taking measures for a strong and stable economy.
- The budget has been focusing on the promotion of domestic manufacturing, as suggested by measures such as expanding Phased Manufacturing plans. The Government has been increasing the import duty on finished goods. It also plans to reduce import duty on the parts used to manufacture finished goods.
- Additionally, the Government is taking non-tariff measures, such as licensing requirements and mandatory compliances, to meet Indian Standards and curb imports of non-essential goods that are available domestically.
- Further, the Central Board of Indirect Taxes (CBIC) has been taking measures to digitise compliances, such as faceless assessment and electronic credit ledger for duty payment under Customs to promote ease of doing business.

Expectations

Expectation #1 Amnesty Scheme for Customs

- To resolve long-standing disputes, clear up the burdened judicial pipeline, and upgrade the law to keep up with the time, technology, and international best practices, the Government should take steps to end long-drawn disputes.
- Under India's indirect tax regime, several litigation matters are pending at different forums involving crores of duty.
- An amnesty scheme, along the lines of Sabka Vishwas or similar schemes, will be a welcome decision. It shall help end long-drawn litigation under Customs. The industry has been waiting for such a scheme for many years to address pending litigation matters under Customs. This will help people, especially small businesses, in getting rid of their past disputes and move ahead with a clean slate.

Expectation #2 Digitalisation of customs litigation process

- At present, the process of adjudication and litigation under Customs is completely physical. Physical submissions of reply to Show Cause Notices ("SCN") and appeals are made before the customs authorities. The documents also require physical signing by the authorised signatories.
- The requirement of physical submission of documents is quite an onerous task and against the Government's initiative of making tax digital.
- Relevant provisions should be introduced in the Customs law to file letters, appeals, and other correspondence with the authorities digitally in line with the GST law.

Expectation #3 Continued exemption of IGST and compensation cess under the MOOWR scheme

- Manufacturing in Customs Bonded Warehouse i.e., the MOOWR scheme, is one of the most promising schemes of the Government. This has provided the impetus to domestic manufacturing. The scheme provides exemption/deferment of duty applicable on capital goods and inputs at the time of import.
- However, Finance Act 2023 made a crucial amendment in the MOOWR scheme by inserting a new Section i.e., Section 65A in Customs Act, 1962. According to the Section 65A, goods can be imported under the MOOWR scheme on the condition of payment of applicable IGST and Compensation Cess at the time of import. Although IGST and compensation cess are creditable, upfront payment of IGST affects the company's working capital.
- While the Section has not been notified yet, the Government should keep the implementation of the said section in abeyance as that will hurt the Government's vision of Make in India. This will also make India a major player in the Global Supply Chain.

Personal taxation

Tapati Ghose
Partner

Current environment

If the personal tax collection is considered a yardstick to measure economic growth, the statistics show 29.53 percent growth compared with the previous year. This year, the government shall present the vote on account before the 2024 general elections. While it may not be the full budget, it is not expected to be a muted one.

If one observes the past pattern of the FM, the focus has been on making structural changes rather than providing tax breaks. Given this, one may expect to focus on the New Tax Regime, faster processing of tax refunds, robust tax collection machinery, and speedy disposal of appeals.

Expectations

Top asks: Ease of tax compliances

- **Expectation #1: Ease of tax payments/obligations for non-residents**

  Simplify the TDS compliance for home buyers where the seller is an NRI

  According to the current provisions, home buyers need to deposit 1 percent of the purchase value as Tax Deducted at Source (TDS), where the property value is INR 50 lakh or more. Although the TDS deposit process is simple and convenient if the seller is a resident (i.e., with the challan-cum-statement in Form no.26QB), the requirements are more complex if the seller is a Non-Resident Indian (NRI).

  In cases where the seller is an NRI, the tax is deducted at a higher rate and the buyer is also required to obtain a TAN, deposit the tax deducted, and file e-TDS returns. While the purchase and sale of the property is not a recurring transaction, obtaining TAN for the mentioned purpose alone may result in having more inactive TANs down the line.

  To address the above-mentioned issue, the TDS process applicable for cases where the seller is an NRI, may be eased by introducing a TDS process that is similar to that of a Resident seller.

  Enabling tax payments from overseas bank accounts (removing the requirement of having a bank account in India)

  At present, tax payments in India are accepted in modes such as net banking, debit cards, NEFT/RTGS, and over-the-bank counter. The tax payment modes have been broadened to include a large number of Indian banks, NEFT payments, RTGS payments, and UPI payments. However, these are possible with an Indian bank only, which makes it difficult for a non-resident taxpayer to make tax payments.

Non-resident taxpayers who need to deposit tax, would benefit if they are allowed to make tax payment from their overseas bank accounts.

E-verification using OTPs to foreign mobile numbers

With the introduction of e-filing of tax returns, efficiencies in time and effort have been brought in. The last mile connectivity of e-filing is the e-verification process that has restricted means. Example: having accounts with net banking/demat facilities with specified banks, Aadhaar OTP to India mobile numbers, digital signature certificates, etc. Non-resident individuals living outside India who need to complete the tax return filing process, could benefit if the e-verification process can be extended via OTP to foreign mobile numbers or having two-factor authentication (different OTPs for foreign mobile numbers and email addresses). This would reduce paperwork and administrative tasks, such as tracking the receipt by the tax office and applying for condonation of delays. Alternatively, the time limit of 30 days should be extended to facilitate verification through physical mode.

Tax refund to overseas bank accounts

Non-resident individuals, especially foreign nationals, who leave India after closing their bank accounts in India, could end up with a refund due to various reasons. At present, the tax refund is payable only to pre-validated India bank accounts. Any delay in processing the refund could cause bank accounts (even if open under the NRO status) to go into dormant mode. This would prevent the refund from being credited to the account. To alleviate the difficulty, foreign bank accounts should be considered for tax refunds in case of PAN-holders registered as non-residents/foreign nationals.

- **Expectation #2: Enhancements to AIS**

Potential to expand the information captured through Annual Information Statement (AIS)

At present, AIS captures information relating to payments where tax is deducted/collected, bank interest, dividends, sale and purchase of capital assets, foreign remittance, refund from the income tax department, etc. This information helps prepare tax returns. The information, collated based on PAN, is reported in AIS to provide a bird's eye view of transactions under the PAN.

However, the information captured is not inclusive of transactions that may be relevant and reported in the tax return. Amongst many transactions where the PAN is quoted, transactions such as Employer Provident Fund, Public Provident Fund, National Pension Scheme, life and health insurance policies, principal, and interest on loan repayment, could be additionally captured to widen the coverage of AIS.

This would help in pre-filling the tax return with the data relating to applicable exemptions, deductions, the taxability of withdrawal proceeds, etc.

Add details to the information captured through Annual Information Statement (AIS)

At present, AIS provides information on the purchase and sale of securities in SFT portions of the AIS from NSDL/CSDL. While this information helps provide a bird's eye view of the transactions made by the taxpayer in securities and mutual funds, it does not serve the purpose of capturing information and ease of data collection to prepare the tax return.

Amongst other information provided in the AIS under this segment, mentioning the date and cost of acquisition, may be useful. This helps in accurate computation of capital gains, without the taxpayer having to go through records for this information.

Policy recommendations and expected impact

Recommendation #1:

Taxpayers are allowed tax credits/other benefits in terms of taxes paid outside India, subject to the fulfilment of certain conditions. As of now, the benefits are available for individuals to claim in their income tax return. Hence, these individuals end up with a huge refund as there is no express provision for the employer to consider the benefit at the time of tax withholding. To provide relief and avoid refund scenarios and related cash flow issues, guidelines can be issued for considering benefits under Section 90 at the time of tax withholding and disclosing them appropriately in eTDS returns.

Recommendation #2:

401K benefit

To provide relief to residents who have income from foreign retirement benefits accounts, a new section has been inserted in the Income-tax Act to defer taxation of income from the foreign retirement fund in the year of receipt. Many countries (the US, the UK, and Canada) tax the income from foreign retirement benefits accounts on a receipt basis. Moreover, to avoid difficulties in claiming the foreign tax credit due to a mismatch in the year of the taxation, the new section can be applied. However, the government may consider enabling this section to be applied retrospectively i.e., it should apply to taxpayers who withdraw from the retiral benefit and their past contributions.

Revised/belated return

- Due date for filing the revised return or belated returns is 31 December of the following financial year.
- In a situation where the assessee is ROR in India claiming a foreign tax credit, it will be difficult to finalise the FTC to be claimed in his India tax return, when the return for the calendar year is not yet finalised in the overseas jurisdiction. For example, in the US, returns for 2024 would be finalised only in April 2025. However, the revised/belated returns can be filed for FY 2023-24 only until 31 December 2024, to claim the credit for taxes paid for the period of Jan–March 2024.
- If there is no extension of due date for belated/revised return filing, the FTC claimed on the return may not be final as it would be claimed on an estimated basis or the taxes withheld at source in the overseas jurisdiction.
- There is a requirement to extend the due date of filing the revised belated/revised return at least until 31 March, instead of 31 December.

Recommendation #3

Bengaluru to be considered as metro city for the purpose of 10(13A)

- The Constitution of India recognises Bengaluru as a metro city amongst other cities, such as NCR, Mumbai, Kolkata, Pune, Hyderabad, and Chennai.
- However, per the Income Tax provisions, only four cities in India (Delhi, Mumbai, Chennai, and Kolkata) are considered to be metro cities and allowed to have 50 percent of the basic salary as the House Rent Allowance (HRA) and 40 percent of basic salary for non-metro cities (other cities).
- Being one of world’s fastest growing cities, Bengaluru provides employment to many. There is an increase in the cost of living in the city compared with other cities. Hence, employees should get a 50 percent deduction for HRA.

Mergers and acquisitions tax

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Current environment

- India has witnessed a sluggish trend during the first nine months of 2023 with M&A activities showing a lower resurgence compared with the previous year on account of multiple global events, such as wars, geopolitical tensions, and fed rates volatility.
- Resultantly, Indian business houses are adopting a cautious approach towards M&A activities as well marquee fund raise activities such as IPO,due to multiple factors, including general elections in the second quarter of 2024. As a result, M&A activities are expected to bounce back soon, thereby creating enormous opportunities for the Indian economy to flourish.
- Considering the above scenario, we have captured the following expectations for the upcoming budget that will help increase M&A activities in the near future.

Expectations

- **Expectation #1: Ensure outbound mergers to be tax neutral**
  - The Companies Act, 2013, permits the merger of an Indian company into a foreign company, subject to certain conditions.
  - An Indian company's merger with another Indian company is tax neutral if the prescribed conditions are satisfied. However, no specific exemption is provided under the Income-tax Act, 1961 for the merger of an Indian company with a foreign company.
  - To encourage cross-border M&A, tax exemption should be provided on the merger of an Indian company with a foreign company by adding a specific clause in Section 47.
- **Expectation #2: Tax neutrality on swap of shares under internalisation**
  - At present, there is an incidence of capital gains tax in India on the swap of shares even in case of internal reorganisations wherein value remains within the group.
  - There is a noticeable rise in "internalisation" through an integration of ownership and consolidation of an entity's value back into India. One of the methods through which such internalisation can be achieved is by way of the swap of shares of the foreign holding company to its wholly owned Indian company and in turn the shareholders of such foreign holding company are issued shares of the Indian company. As a result, shareholders directly hold the Indian company, which in turn holds the foreign company.
  - Considering there is no third-party transfer and value remains within the group, a specific provision to exempt the above swap of shares shall help boost shareholders' confidence and strengthen the Indian market by way of consolidation of value in India.

- **Expectation #3: Extend the transition of losses from amalgamating a "non-industrial undertaking" company to an amalgamated company**
  - Under the existing provisions in Section 72A, the benefit of carry forward of losses and unabsorbed depreciation is, inter alia, allowed in cases of amalgamation of a company owning an "industrial undertaking".
  - The provision was incorporated when India was a capital-intensive country. The country is moving from a capital-intensive to capital-light model; the services industry is also growing and contributing to the economy.
  - To encourage rapid consolidation and growth, and make India competitive in the services sector, the benefit under Section 72A (to carry forward losses and depreciation on amalgamation) should be extended to service industries amongst others.
- **Expectation #4: Provide exemption to foreign shareholders in case of mergers and demergers**
  - In case of merger of the foreign company (Co A) deriving substantial value from India, [which holds the Indian company (Co B)], with another foreign company (Co C), Section 47(via) provides that transfer of shares of an Indian company (Co B) transferred in a foreign amalgamation would not be regarded as a transfer, provided certain conditions are met.
  - In case of merger of the foreign company (Co A) deriving substantial value from India, (which holds another foreign company (Co B) deriving substantial value from India), with another foreign company (Co C), Section 47(viab) provides that transfer of shares of a foreign company (Co B) that derives value substantially from assets located in India, in an amalgamation, would not be regarded as a transfer, provided certain conditions are met.
  - The above sections seem to indicate that the exemption is provided only to the amalgamating foreign company and not to its shareholders.
  - Specific provisions, such as Section 47(vii), should be incorporated in the Act to provide relief to the shareholders of the amalgamating foreign company (shareholders of Co A). The provision exempts shareholders in a domestic amalgamation.
  - A similar issue emerges for demergers. In the absence of exclusion from compliance with the Indian company law requirements in Section 47(vid), the benefit of shareholder exemption is not available to shareholders of the foreign demerging company in an overseas demerger. This has the effect of imposing a tax liability on the shareholders of the foreign demerging company and hence, against the principle of enabling tax neutrality for overseas demergers.
  - A proviso [as provided in Section 47(vid) and 47(vid)] should be incorporated in Section 47(vid) to provide an exemption to the shareholders of the foreign demerged company despite the demerger not complying with the relevant Indian company law provisions.
- **Expectation #5: Provide exemption to the Indian holding company on an overseas merger of two foreign subsidiaries**
  - An overseas merger between two foreign subsidiaries of an Indian holding company is undertaken for reasons, such as consolidation, value creation, and regulatory hurdles. While the value is retained within the group on such overseas merger, there could be tax implications in India for the common Indian holding company whose shares in amalgamating foreign company are transferred pursuant to overseas merger with another foreign subsidiary company.
  - There should be tax exemption for such Indian holding company in case of transfer of shares of the amalgamating company in exchange for amalgamated company shares pursuant to the merger of its foreign subsidiaries.
- **Expectation #6: Enforce complete tax-neutrality on mergers and demergers**
  - Section 56(2)(viib) seeks to tax a company (other than a company in which the public are substantially interested) on issue of shares for a consideration higher than the prescribed FMV.
  - While there is a specific exemption from applicability of section 56(2)(x) to the shareholders on receipt of shares on tax neutral transactions, such as mergers/demergers, no specific exemption is available u/s 56(2)(viib) for a company issuing shares.

- To provide tax neutrality for mergers/demerger transactions with respect to shares issued by the amalgamated/ resulting company, an exemption should also be provided under section 56(2)(viib) for the issuance of shares for qualify mergers/demerges.

- **Expectation #7: Rationalise taxation of contingent consideration**
  - India is an attractive market for international investors. With a focus on balancing profitable exits and correct valuations, most private equity players plan to introduce a combination of clauses in the shareholders agreement. This includes consideration payable in a contingent manner based on certain performance milestones that the promoters achieved.
  - In essence, such clauses incentivise promoters for their better performance after the deal.
  - There is no clarity on whether such contingent consideration is to be taxed in the year of transfer or receipt, after the consideration crystallises. It may be clarified by an explanation or clarificatory provision to Section 45 (in case of a contingent consideration) that the contingent portion should be chargeable to tax as capital gains in the year in which it is crystallised, irrespective of the year in which the transfer takes place (in line with the accrual concept - refer to Section 5 of the Act).

Transfer pricing

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Sanjay Kumar
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Current environment

The transfer pricing regime in India is now more than two decades old. Most of the basic transfer pricing principles and practices have almost settled. There is sufficient judicial guidance in the domain. The government has also adopted various globally accepted best practices to provide trust and confidence to foreign investors and prevent disputes. Safe harbour rules, Advance Pricing Regime, effective MAP programme, adoption of the sixth method for transfer pricing analysis, etc., are a few examples. Transactions such as intra-group charges, payment of variable royalty, and cross-border business arrangements, are becoming common. Transfer pricing has also changed due to the recent changes brought by OECD through the BEPS guidance.

These complexities require deliberation by the government. Moreover, some legal anomalies and practical difficulties remain in the transfer pricing regime; these anomalies may need necessary amendment in the law during the budget process.

Expectations

Top asks

- **Expectation #1: Easing compliance requirement for transactions by non-residents**
  - Following amendment in Section 115A of the I-T Act, 1961, a non-resident taxpayer is not required to file income tax return in India if it is assessable to tax in India for dividend, interest, royalty or fee for technical services. Taxes have been appropriately withheld from such taxable income under the provisions of Chapter XVIIA of the Act.
  - With the above exemption for filing income return, a question often arises about the taxpayer's obligation for filing Accountant's Report in Form 3CEB under section 92E of the Act. This is because Section 92E has not been amended consequent to the above-mentioned exemption. Non-reporting of international transactions in Form 3CEB attracts multiple penalties under Sections 271BA, 271AA, 271G and 270A of the Act. Consequently, a situation arises where a non-resident need not file a tax return in India but would still need to file Form 3CEB to avoid any penalty for non-reporting of the international transaction. This is an unnecessary compliance burden for non-resident taxpayers.
  - Further, after the abolition of dividend distribution tax, dividend income is taxable in the hands of shareholders. A non-resident shareholder receiving dividend may still require filing Form 3CEB in case the conditions under Section 115A would not be satisfied. However, dividend payment by a company is an appropriation of profits and arises out of corporate action. Hence, the arm's length price of dividend is not determinable and is not technically covered under transfer pricing. The law should specifically provide exemption for the list of transactions such as dividend and bonus shares etc. which are not covered under transfer pricing and hence, transfer pricing reporting and compliance is not required for such transactions.

- **Expectation #2: Streamlining Advance Pricing Agreement (APA) scheme to expedite resolutions and remove certain anomalies in law**
  - Speedy APA conclusion - India has a huge inventory of pending APA applications and the average disposal rate is slow. This is primarily attributable to limited allocated resources with appropriate experience to review and conclude APAs. Delay in APA resolution results in multiple challenges for the taxpayer and the government. The taxpayer has to continue with litigation, along with APA, which results in duplication of time and resource. It also increases interest cost on APA adjustment, compromising the taxpayer's negotiating position from the effective tax cost perspective. The huge inventory also affects the APA team's effectiveness and efficiency.
  - Mechanism for corresponding tax adjustment and withholding tax refund for AE on conclusion of bilateral APA - The APA scheme does not provide for corresponding tax adjustment in the hands of the associated enterprise based on the agreed arm's length price under the bilateral APAs, resulting in excess withholding tax in India.
  - If the arm's length price determined in the APA is lower than the actual service fee accrued to the taxpayer, the Indian taxpayer is required to claim lower deduction for such intra-group payments in the modified return for the past covered years and rollback years. This often results in excess withholding tax for the non-resident AE. There is no mechanism for the refund of withholding taxes to non-resident taxpayers.
  - Removal of restrictions under section 92(3) for unilateral APAs - Section 92(3) of the Act is a restrictive tax provision. Under this provision, the taxpayer's taxable income already reported in the tax return cannot be reduced or losses cannot be increased on account of transfer pricing adjustment. This provision was primarily introduced for transfer pricing audits. APA is a dispute prevention mechanism. Restrictions under section 92(3) should not apply to APA resolutions.
- **Expectation #3: Revision of safe harbour rules to reduce litigation of small/medium companies**
  - Existing safe harbour rules have been restricted to very small companies, making them inaccessible to medium-scale companies. Safe harbour rates are higher than the comparable benchmark, making it commercially unviable for taxpayers to adopt. Therefore, taxpayers will continue to face the risk of litigation or apply for APA to attain tax certainty. This increases the APA inventory. The APA should primarily involve cases with complex transactions and business models that require in-depth business and economic analysis to set transfer prices.
  - The government may re-evaluate the safe harbour provisions on the following three aspects: (a) reduce the class of transactions from the safe harbour and restrict it only for IT, ITeS, and business support; (b) provide the safe harbour rates closer to comparable benchmarks with a little premium for certainty; and (c) increase the threshold to cover almost 75 percent of the companies under this spectrum. This can serve the dual purpose of providing tax certainty to taxpayers and easing the APA burden.

Expected impact

- **Recommendation #1:** Section 92E should be amended to provide exemption to non-residents from filing 3CEB for transactions they are exempted from filing tax return under Section 115A of the I-T Act, 1961.
- **Recommendation #2:** The APA scheme should be amended to provide for the following:
  - The mechanism to fast-track APA resolutions and provide for time bound APA resolutions, at least for captive entities. Captive entities cover between 35 percent and 40 percent of the APA applications
  - Removal of restrictions under Section 92(3) of the I-T Act for effective negotiation and balanced APA outcome
  - Provide a mechanism for corresponding adjustment in the taxable income of non-resident AE on conclusion of bilateral APA.
- **Recommendation #3:** To provide effective safe harbour rules based on the present economic scenario and comparable benchmarks in India

Identified Themes

Supply chain

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Current environment

India's participation in Global Value Chains (GVC) experienced steady growth from the 1990s to 2008, peaking at 47.6 percent of the total exports before the 2008 global financial crisis. However, by 2022, this figure declined to 39 percent. India's GVC involvement primarily focuses on forward linkages, centered on the export of raw materials and intermediate inputs, with sectors such as metals and refined fuels having high participation rates but limited value addition.

Notably, India has seen increased GVC participation in the medium-to-high technology manufacturing sectors between 2017 and 2022. These sectors include chemicals, electrical machinery, industrial equipment, and transport equipment. This suggests a positive move towards increasing value addition in intermediary goods.

Sectors with potential to enhance backward linkages (increased domestic value addition) include industrial equipment, electrical machinery, telecom, and automobiles. Despite exporting smartphones, the telecom sector has limited involvement in manufacturing intermediary parts, keeping its GVC participation low.

To build competitive value chains in India, discovering mineral wealth and identifying areas of its potential by use of advanced technologies are essential. A recent study by the Centre for Social and Economic Progress (CSEP)[1] (conducted on 49 non-fuel minerals, including rare-earth for computing the criticality in India), revealed that categorisation of critical mineral depends on several factors, such as availability, monopoly on resources, use for frontier technologies/clean energy, substitutability, supply risk, recycling, and GVA multiplier. Based on the assessment on economic importance and supply risk by the joint committee of CSEP, Council on Energy, Environment and Water (CEEW), and other ministerial departments, a comprehensive list of 30 minerals is found to be most critical for India. The associated value chains with the highest potential to increase GVA multiplier, based on 30 critical minerals are mentioned below:

- Clean technologies, including Zero-Emission Vehicles (ZEV), wind turbines, solar panels, advanced batteries, hydrogen fuel cells, and small modular reactors
- Information and communication technologies, including semiconductors
- Advanced manufacturing inputs and materials such as defence applications, permanent magnets, ceramics, high value-added metals, electronic materials, composites, polymers, and biomaterials

The import risks of critical minerals may be reduced by developing resilient supply chains, signing trade agreements, and acquiring mining assets abroad.

[1] https://mines.gov.in/admin/storage/app/uploads/649d4212cceb01688027666.pdf

Expectations

Top asks

- **Expectation #1: Increase budget allocation for Research and Development (R&D) activities to increase competitiveness in the high-technology manufacturing sectors, such as semiconductors, medical devices, defence and aerospace, clean technologies, and intermediary goods manufacturing advanced manufacturing inputs and materials**
  - India's investment in R&D has remained stagnant at 0.6-0.7 percent of GDP from FY 2013-14 to FY 2020-21, a stark contrast to the 2-4 percent allocation observed in other major economies. In terms of Gross Expenditure on R&D (GERD), India's allocation is one of the lowest globally, standing at about 0.7 percent, whereas comparable countries, such as Brazil, Russia, China, and South Africa spend 1.2 percent, 1.1 percent, above 2 percent, and 0.8 percent, respectively. The world average is 1.8 percent.[2]
  - There is need for expedited exploration, overseas mineral acquisition, resource efficiency, recycling of minerals, and finding substitutes for critical minerals through suitable R&D. R&D on opportunity for production vanadium has to be strengthen to ensure the availability of – one of the 30 critical minerals essential in value chain of clean technologies.
  - While recent government initiatives lay emphasis on R&D, the predominant focus remains on attracting investments for manufacturing. The recent introduction of the Promotion of Research and Innovation in the Pharma MedTech Sector (PRIP) is a positive step. To bolster India's global R&D standing, the implementation of a comprehensive National R&D policy to enable innovation and development of IP in India is crucial. GERD targets should be reviewed in line with the country's aspirations of becoming a US$ 5 trillion economy.
- **Expectation #2: De-risking of credit inflows to MSMEs in the manufacturing sector for capital investment and skill development to develop the capability for advanced manufacturing of intermediary goods**
  - To reduce risks in capital flows to MSMEs, particularly in industries such as automotive, electronics (manufacturing of ICs), industrial and electrical machinery, and chemicals (that saw over 5 percent export growth from 2017 to 2022), it is advisable to promote risk mitigation tools, such as credit guarantees and insurance schemes.
  - Recent data from the Reserve Bank reveals 13.2 percent credit growth for medium-sized industries in June 2023 (compared with 47.8 percent the previous year), with the micro and small industries experiencing a 13 percent increase (compared with 29.2 percent the prior year).[3] Despite ongoing credit accessibility initiatives, there remains a significant need for innovative solutions to address the credit gap faced by MSMEs.
  - As on 1 April 2023, the Credit Guarantee Scheme for Micro and Small Enterprises raised the credit limit from INR 2 crore to INR 5 crore, along with a 50 percent reduction in annual guaranteed fees. However, the Expert Committee on Micro, Small, and Medium Enterprises estimated the MSME credit gap to be between INR 20 and INR 25 lakh crore.[4] Substantial efforts are still necessary to bridge this gap in support of MSMEs.
- **Expectation #3: Investment promotion schemes to attract increased greenfield investment in manufacturing and export of intermediary goods**
  - Foreign Direct Investment (FDI) represents an important internationalisation pathway to Global Value Chain (GVC) participation. Several measures taken by the government, including the implementation of a goods and services tax, a reduction in corporate tax rates, steps to ease regulatory compliance, initiatives to promote domestic manufacturing through public procurement, the Phased Manufacturing Programme (PMP), and the Make in India program, have contributed to a 57 percent increase in FDI equity inflows into the manufacturing sector between 2014 and 2022, compared to the previous eight years (2006-2014).[5] This momentum needs to continue to ensure India improves upon the backward linkage GVC participation.

[2] https://dst.gov.in/sites/default/files/R%26D%20Statistics%20at%20a%20Glance%2C%202022-23.pdf

[3] https://economictimes.indiatimes.com/industry/banking/finance/banking/bank-credit-growth-to-msmes-decelerates-in-q1-rbi-data/articleshow/102471492.cms

[4] https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/EN/wasme_access_to_credit_for_indian_msmes.pdf

[5] https://pib.gov.in/PressReleasePage.aspx?PRID=1947211#:~:text=Due%20to%20Make%20in%20India%20Initiative%2C%20FDI%20equity%20in%EF%AC%82ow%20in,Departments%20and%20various%20State%20Governments.

– The Production Linked Incentive (PLI) scheme has been instrumental in attracting investments to bolster domestic manufacturing competencies across diverse sectors. The forthcoming initiatives (could be in capital machinery, electricals, white goods, chemicals, etc.) — whether under the PLI umbrella or an alternative framework — should focus on overall ecosystem development through progressive localisation and an effective implementation based on sector potential and local supply chain maturity.

Policy recommendations and expected impact

- **Recommendation #1: Rationalisation of duty rates for import of critical minerals required by EVs and related components**
  - NITI Aayog set a 2030 target for EV sales to make up 70 percent of commercial car sales, 30 percent of private car sales, 40 percent of buses, and 80 percent of two-wheelers and three-wheelers. Additionally, the country would need to develop its public charging infrastructure. To ensure this, critical minerals, such as lithium and indium, require focus on securing supply chains and acquire foreign mineral assets to ensure their continuous supply.
  - The Manufacturing & Other Operations in Warehouse (MOOWR) scheme, pursuant to Section 65 of the Customs Act, 1962, presents a sophisticated mechanism for exporters procuring raw materials and capital items, allowing for the deferment (and, in effect, exemption if finished goods are exported) of duties. Further steps can be taken to improve the on-ground implementation of this scheme by simplifying compliance requirements. In addition to ensuring that customs duties are deferred on import of goods, the scheme should remain at par in terms of other benefits and schemes applicable for a normal unit.
- **Recommendation #2: De-risk the import of critical minerals required in the production of clean technologies to meet the policy agenda on climate change mitigation**
  - While India would need to rely on imports for these technologies over the next two decades, further work must be done to better use the available minerals within the country for its longer-term needs. Newly installed renewable capacity will require replacement after two-to-three decades. India can be better prepared for the next stage of green technology use by laying the groundwork for exploring and mining. Investment towards further exploration on critical minerals, such as cobalt, molybdenum, and nickel are essential. These are the critical minerals used in the value chain of clean technologies; further R&D for their exploration is essential. There is no reserve of these minerals, but it is estimated that there will be collective reserve requirement of ~200 KT by 2040.[6]
- **Recommendation #3: Provide greater credit access to MSME to enhance their capability in advance manufacturing for the semiconductor, medical equipment, and industrial equipment segments**
  - The RAMP scheme launched in July 2022, will help MSMEs to access credit by providing them guarantees and collateral support. This will make it easier for MSMEs to obtain loans from banks and other financial institutions. In addition to this, recommendation is towards providing benefit of ease of access to credit specific to capital investment aimed towards adding advanced technology in manufacturing operations specific to high-growth sectors, such as semiconductor, medical devices, automobiles, and chemicals. Only 15–20 percent of the MSMEs have access to formal credit. Greater formalisation could see demand for formal credit jump by 30–50 percent.

[6] https://csep.org/wp-content/uploads/2021/12/Critical-Minerals-for-Green-Technologies-1.pdf

Artificial intelligence

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Current environment

- Driven by the global buzz around AI and analytics, India's tech and digital talent, and push from the government, India is emerging as a powerhouse in this area. Estimated to grow at a year-over-year CAGR of more than 30 percent, India Inc. has adopted AI in various segments. India might be behind a couple of global matured markets, but far ahead amongst developing economies. The application of AI brings in 3–10X improvement in business processes. Hence, if used effectively, the technology will have a significant contribution to India's ambitious goals of reaching US$ 5 trillion economy.
- The central and multiple state governments have launched various schemes to push the AI adoption in India. Some of these schemes/initiatives are "AI for all" by Niti Ayog and Chair at GPAI in the current G20 summit. MeitY also plans to launch IndiaAI, Bhasini Programme, and YuvAI for skilling Indian youth by the central government. Similarly, multiple state government schemes (notably Tamil Nadu, Telangana, and Karnataka) have been launched to grow and develop skills, propel India Inc and investments in this area, and regulate and govern the use of AI.
- While multiple initiatives have been introduced to make India a global AI hub, a few areas need to be considered. First, accelerate programme execution. AI research and such programmes are being launched by almost all mature countries. It is a topic of innovation where speed (and possibly that is the only thing) matters. Second, start reaping the benefits by launching specific programmes under Public-Private Partnership (PPP) with crowd-sourcing ideas, strict timelines, and scaled-up solutions for the country. Third and possibly most critical is the focus on the two foundational elements of AI – data (collection, storage, and analytics) and trustworthy use of AI.

Expectations

Top asks

- **Expectation #1: Accelerate research and development for use of AI in various areas, including tax**
  - While research publications and patents in this area have improved from India, we are still way behind in terms of innovation, citation index, and global exposure. The government should boost investments in AI and identify new research areas, such as quantum computing in AI, digital nudge for social good using AI, Explainable AI (XAI), Gen Chem and Computational Biology, and smart and connected cities. Governments' role in promoting academia-industry collaboration will be key. Choosing one or two of the transformational areas mentioned above that still need solutions and require a faster path to completion.
  - A dedicated pool of officers across direct and indirect taxes should have requisite knowledge of AI and its use. This will enable them to use AI in tax assessment, tax administration, and taxpayer facilitation. In the long run, use of AI by tax officials will help focus on non-compliant taxpayers, including early detection of non-compliance trends and taking preventive measures.
- **Expectation #2: Promote PPP model with value-based implementation**
  - India's AI strategy focuses on social impact and has called out three sectors as a priority – agriculture, education, and healthcare. The key is to identify specific use cases that the government can implement; these cases should have the maximum impact on the society at large. List the key challenges in these sectors, crowd-source ideas, implement those

ideas (possibly under the PPP model with value-based impact), and scale the solution to be the service provider to the globe. Some ideas could be the ones mentioned below:

- Digitising lawsuits and judgements in the tax area, and implementing a triage model using efficient reviews on tax, property, marital, and other easy-to-review litigations.
- Using lifestyle-based data to predict future health score (disease propensity models) for the population to reduce the burden on healthcare and proactive mitigation
- Digital nudge using AI to prevent fraud on government schemes, financial and tax-related transactions, and social issues, such as Swatch Bharat
- Quality education in local languages for rural India using LLMs specific to Indian languages possibly under the national language transition mission
- Use of satellite images from ISRO on the crop insurance claims process to make it easy for farmers

- **Expectation #3: Focus on centralised data repositories for the country**
  - India has taken various significant steps in this area with Adhaar, CoWin, portability of insurance policies, and multiple other initiatives. However, to boost AI and analytics further, we need to take the following steps:
    - Improve the trust of customers and organisations (locally and globally) that this data is protected and secured. We must change the negative perception and narrative that may exist today.
    - Completeness of data in several areas, such as having an Electronic Health Records (HER) and centralised medical record database such as those in other mature countries for effective healthcare solutions
    - Limited but allowable access to the data for research, crowd-sourcing new ideas, and use by industry (using the latest tools, such as creating and opening model APIs and split learning)

- **Expectation #4: Focus on trustworthy AI**

  Establishing a governance mechanism is crucial to ensure trustworthy AI, covering everything from data sourcing and storage to the application of AI methods. This is a challenging task, particularly in advancing research and creating intellectual properties, especially considering India's diverse landscape.
  - Defining governance and creating frameworks on several areas, including the ones mentioned below, are crucial:
  - Data privacy and accountability
  - Transparency, attributability, reliability, and robustness of models
  - Fair and impartial use of tools
  - Safety and security of technology stacks
  - Ownership of results

Policy recommendations and expected impact

- **Recommendation #1:** Although the Digital Personal Data Protection Act (DPDP) is a great beginning, the industry needs a deeper dive to ascertain how each industry is using personal data and keeping a balance between fostering innovation and regulating data use. AI is still in its nascent stages in many ways. We have seen many good and unethical/fake/wrong uses of the technology. India must introduce penalties for unethical use, helping it shape up its image as a global AI hub. India's diversity, cultural identity, and values should be considered while drafting policies on AI.
- **Recommendation #2:** Craft a committee/programme that will task each government department to prioritise innovation using AI in their respective areas. Work with research, industry, academia, or other departments, and craft a value-driven PPP model to initiate time-bound solutions. This will boost the economy and foster innovation using ethical principles.
- **Recommendation #3:** Due to complexities, tax litigation takes several years to reach finality. Moreover, a significant amount of money is locked up in litigation. The use of AI technology to sharpen the tax administration's decision-making process, around filing or not filing an appeal, based on key parameters. With the use of Generative AI, tax administrators can summarise tax positions based on facts of the case, legal interpretations, and views of the courts. The use of AI can also help assess winning/losing probabilities for a case, for the tax administration. This can help authorities decide whether to pursue a particular case in litigation or not. AI can help decide whether to litigate a case and optimise the number of cases, saving time and energy of the tax administration. The number of lawsuits can also decrease significantly, reducing the pressure on the legal system.
- **Recommendation #4:** Design a central committee of AI/ML experts in India whose role will be on standardising the curriculum for masses and suggesting/investing on new unexplored technologies. Collaborate with leading academic and industry players to develop and globalise solutions, starting locally in India and using Indian IP.

Ease of doing business

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Current environment

- Ease of doing business is improving on regular basis based on accelerated reforms undertaken by the government since pandemic. Some of the key developments and reforms have been, among others, through digitisation drive, availability of high-speed broadband connectivity for the villages, physical infrastructure push, higher installed renewable energy capacity, establish process for thoughtful financial regulations, relax controls overs corporate downsizing, improving direct benefit transfers, etc.
- Starting with a 98-point Reform Action Plan in 2014, Business Reforms Action Plans (BRAPs) over years has covered more areas of reform. BRAP 2022 comprises two parts: Business Centric Reforms (Action Plan A) and Citizen Centric
- Reforms (Action Plan B). Business centric reforms bring attention on land administration and transfer of land and property, labour regulation enablers, construction permits enablers, etc. Citizen centric reforms cover services such as online single window, certificates, obtaining utility permits, public distribution system, transport department, etc.
- Developing online systems for licensing, simplification of application forms, reducing timelines for issue of licenses, increasing validity of licenses, provision for self-certification, third-party verification, are some of the minimizing mechanisms used for burdensome compliances. A reduction in regulatory compliance burden on businesses and citizens has the potential to become the new driver of economic growth. Reduced compliance burden will especially help small firms that account for over 95 per cent of Indian businesses.

Expectations

Top asks

- **Expectation #1: Accountability**
  - Specific measure: The National Single Window System launched by the government in 2021 made impressive progress. It added a few central government departments and some states. However, more seamless integration between states and the central government is desirable. As some states are still not part of the process, a legislative framework would bring timely service delivery, accountability, and certainty to actions, and transparency in achieving the objective and purpose.
  - Measurable outcome: Improved service delivery, accountability, and certainty of actions
  - Rationale: About 626 central-level approvals are offered through the National Single Window System (NSWS).[1] The absence of legislative backing for these clearances leaves room for deviations and delays in the provision of approvals. Enacting legislation for these services through NSWS will promote greater transparency in the system.

[1] As on 06 November 2023

- **Expectation #2: Institutional mechanism**
  - Specific measure: The Department for Promotion of Industry and Internal Trade (DPIIT), in coordination with central ministries/departments, states, and Union Territories (UTs), has spearheaded reforms to improve the business regulatory environment in the country. Currently, India lacks structured mechanisms to regularly improve the business delivery system. Establishing an institutional mechanism involving central and state governments can continuously help improve the process that the government has started.
  - Measurable outcome: Improved service delivery
  - Rationale: Establishing an inter-state council to monitor the National Single Window System will help improve the system, bring accountability, and improve the service delivery. This aims to ensure that states actively participate in improving service delivery and that India maintains a conducive FDI environment and seamlessly implements policy reforms.
- **Expectation #3: Process reforms**
  - Specific measure: Introducing the National Single Window System has been a major step forward. The process needs to be strengthened for reforms that impede manufacturing, trade, and investment. Regular and continuous reforms are required for accelerated economic growth. Reforms are not only required for the domestic extent but also uniformity across the country. These reforms are also soon to move to international standards and best practices.
  - Equally important to have information on the process and timelines
  - Measurable outcome: National-level and time-bound delivery of services
  - Rationale: The reforms in the country are not uniform. This has created unwanted migration, uneven development, and socio-economic challenges. To address the delays in approving key clearances required for business establishment, a mechanism for deemed approvals and parallel processing of clearances should be implemented. This would ensure that departmental delays do not impede the business setup process. Further, these process reforms should be backed by the legislation mentioned in Expectation #1.

Trade 4.0

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Current environment

- Ongoing digital transformation and integration of advanced technologies are reshaping global supply chain and trade. These technologies encompass Artificial Intelligence (AI), machine learning, and blockchain, collectively referred to as Trade 4.0. They have the potential to improve the resilience of supply chain and enhance efficiency of the international trade.
- They offer a broad spectrum of advantages, such as reducing trade expenses and complexity, promoting resilience and sustainability, and facilitating the involvement of developing countries, and Small to Medium-sized Enterprises (MSMEs) in the global supply chain and trade.
- Different countries have different digital maturity and engagement. This originates from variations in digital infrastructure and the adoption of these technologies. Furthermore, issues related to digital trade such as interoperability challenges and differences in regulations governing cross-border data flows, can impede the widespread adoption of Trade 4.0.
- The digital transformation of global trade through Trade 4.0 technologies offers numerous benefits. However, disparities in digital maturity, infrastructure, and regulatory frameworks can pose obstacles.

Expectations

Top asks

- **Expectation #1:** Promote development of legal and tax frameworks that enhance transparency and streamline business operations, adapting and evolving alongside technological progress, leading to Trade Facilitation 2.0.
  - Encourage trading partner nations to collaborate and include in the trade agreements Technology 4.0 enablement to promote trade and supply chain development by enabling seamless cross-border data flows, ensuring to improve cybersecurity and improve legal regulations
  - Enable the creation of interoperability in standards and protocols to digitise and exchange data, thus streamlining and promoting efforts towards data standardisation to achieve interoperability while safeguarding confidential business information
- **Expectation #2:** Accelerate the digital journey and encourage technology adoption by industry segments to increase trade and improve operational efficiency.
  - Establish requisite digital infrastructure and drive technology adoption to accelerate cross-border trade and encourage investments in emerging economies and underserved regions, including mobile money infrastructure
  - Focus on incubating digital skills and trade expertise through knowledge and skill centres
- **Expectation #3:** Promote establishment of interoperable standards and protocols to digitise and exchange data to simplify digital trade transactions.
  - Encourage ongoing digitalisation of border procedures and creation of smooth customs corridors and other border agencies.
  - Promote international awareness by sharing insights and guidelines regarding potential technologies, including the best practices for their implementation.

Technology stack/digital infrastructure

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Current environment

India's technology stack and digital infrastructure have undergone a paradigm shift in the past 10 years. Backed by the Government of India's sustained impetus towards digitisation, several governance operations have been automated and simplified to further improve the ease of doing business in India. In this context, two critical areas of transformation stand out – service delivery to citizens and tax administration.

Service delivery

- By architecting and enabling the India Stack and associated initiatives, the government has put in place a robust digital public infrastructure that has simplified and eased citizen service delivery. The infrastructure has also brought down the cost of several critical operations, such as opening bank accounts, digital payments, targeted delivery of subsidies, and identity and document verification.
- Apart from enabling ease of governance in India, the country's approach to digital public infrastructure is now on the verge of being "exported" to geographies beyond India; Article 56 of the G20 New Delhi Leaders' declaration is a testimony to the same.

Tax administration

- Communication with taxpayers has been streamlined with paperless correspondence, faceless assessments and appeals, and structured tax portals. The tax administration focuses on digitising compliance and increasing the tax base and tax collections.
- The tax administration has been aggressive in introducing technology and automation in tax, acting as a booster for taxpayers to adopt technology for compliance and reporting. This has made their internal processes more efficient. With the growth of the Indian economy and its tremendous potential, the government may consider the next phase of technology reforms. Some of these are discussed below.

Expectations

Top asks

- **Expectation #1: Unified digital infrastructure to use filings under different regulations to reduce multiple reporting and reconciliation of the same/similar data**
  - Taxpayers are required to do multiple filings/reporting under different legislation, such as tax laws (direct and indirect), company law, and foreign exchange regulations. It is often seen that the same/similar type of data is filed with different authorities under aforesaid laws.
  - The government may consider streamlining and unifying their digital infrastructure such that data filed under one legislation/with one authority, is automatically used for reporting under different legislation. For example, (1) financial data (balance sheet and profit and loss statement) that needs to be mentioned in the Income Tax Return Form, can be sourced directly from filings under company law; (2) GST data in clause 44 of Form 3CD (Tax Audit Report) can be sourced from GST returns.
  - In the long term, information required by tax and regulatory authorities could be centralised. Each authority can pull out relevant data from the data pack shared by taxpayers. The Standard Audit File for Tax (SAF-T) discussed below, could be a good starting point for initially centralising tax requirements (income tax and indirect taxes). This will save taxpayers from multiple filings of the same/similar data. From a regulator's standpoint, the move will ensure consistency in reporting data to the authorities.
- **Expectation #2: Standard Audit File for Tax (SAF-T)**
  - At present, the tax auditor is responsible for the primary level of data collation/check around the tax attributes of a taxpayer during conducting tax audits. Taxpayers typically use different ERP systems to maintain books of account. Often, the taxpayers manually extract data and provide to the tax auditors for validation. Further, during assessments by the tax administration, taxpayers collate and submit the data and thereafter tax officers evaluate them. These are also manual processes. Often, the same data is sought by administrators responsible for different pieces of legislation, such as income tax and indirect taxes. In this process, the possibility of inadvertent errors, and delays and inconsistencies in reporting and data verification cannot be ruled out.
  - The tax administration may consider introducing SAF-T, which is a global OECD standard and has been adopted by many European countries, for both, direct and indirect taxes. SAF-T involves creating a data file containing business accounting transactions in a standardised format. This benefits taxpayers as the process of data submission to tax authorities can be automated. From the tax administration perspective, a SAF-T file could significantly enhance and automate the tax audit process on a near real-time basis, with the least interference for taxpayers.
  - The implementation of SAF-T will catapult tax digitalisation to a higher level and significantly reduce the time and effort of tax administration and taxpayers.
- **Expectation #3: New Digital Public Infrastructure and open networks**

  India's commitment to create and enable Digital Public Infrastructure (DPI) not only unlocks innovation but also has the potential to transform structural problems in several sectors. In line with the previous Budget announcements that provided the direction towards such an approach for sectors including agriculture and health, and for the creation of Digital Public Infrastructure (DPI) can be a shot in the arm for the nascent DPI/Digital Public Goods (DPG) ecosystem in India. Some of the focus areas could be as follows:
  - **Geo-spatial analytics:** In recognition of the diverse geographical and infrastructural challenges across India, and the vision set in the Indian Space Policy, 2023, a Budget announcement for an open network for geo-spatial analytics could unlock innovation in the space economy. This would act as a catalyst for several focus segments, such as urban planning, agricultural practices, disaster preparedness, and transportation, with an emphasis on tailoring solutions for the unique needs of different regions.
  - **Purple economy:** Specific initiatives targeting differently abled citizens can go a long way in ushering in a new era of inclusive governance and realise the untapped potential of the purple economy. Earmarking funds for a DPI-led approach for research and development in healthcare and assistive technologies and training programmes suited to integrate the differently abled population into the workforce, will help unlock untapped resource potential.

- **Online dispute resolution:** Resource allocation for a phased rollout of an open network for online dispute resolution, beginning with small commercial disputes, may further unlock innovation in the sector. Recognising the diversity of India's legal landscape, focus should be on piloting these systems in select high-demand sectors, expanding their scope gradually. This can reduce the burden on the Indian judicial system and trigger a fast-tracked resolution mechanism.

  In the era of open networks and shift from platforms to protocols, the government has recognised the importance of DPI in enabling cross-border data flows with trust strengthening bilateral relationships and the inter-operability of national systems for collective benefit. Directions towards the creation of a **Global Digital Public Infrastructure Repository (GDPIR)** in line with **Article 56 of the G20 New Delhi Leaders' Declaration,** and budgetary commitment to build capacity, provide technical assistance and adequate funding support to implement DPI beyond India. These developments can formally place India as "Viswa Guru" in digital governance.

Policy recommendations and expected impact

With the enactment of the Digital Personal Data Protection Act, 2023, India entered a new era of data economy. Several provisions in the Act will need guidelines and rules for operational clarity and seamless implementation. Framing and notifying rules will be beneficial for the industry.

Space

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Current environment

- The past year has been nothing short of exhilarating for India's space industry. The Indian Space Research Organisation (ISRO) has garnered national pride and enthusiasm with its remarkable lunar and solar missions, captivating the imagination of the nation. However, the excitement did not stop there; it marked the onset of numerous strategic initiatives. These included the transfer of space technology to the private sector and the forging of significant international co-operation agreements, such as the Artemis Accords and the Critical and Emerging Technology (iCET) initiative. Moreover, the sector witnessed an unprecedented influx of private investments,[1] reaching record levels across segments to affirm its significance.
- This extraordinary surge in space-related activities was strategically timed, dovetailing with the introduction of the India Space Policy in 2023. This landmark policy ushered in the active participation of Non-Government Entities (NGEs) in core space endeavours and meticulously outlined a visionary roadmap for India's burgeoning space economy. An integral part of this transformative journey is the Indian National Space Promotion and Authorisation Center (IN-SPACe), which unveiled a 10-year strategy for the nation's space sector. The audacious vision for the sector stands at an impressive US$ 44 billion by 2033.[2]
- While 2023 has offered a glimpse into the promising future of the space sector, it is crucial to underscore the nascent nature of the private and non-government segment within this domain. Achieving the ambitious vision set forth in the India space policy necessitates the orchestration of a series of strategic government initiatives. These measures are indispensable in enabling sustained growth and fostering a culture of innovation within the sector, where private enterprises are set to play a pivotal role.
- As the space sector continues to evolve, it serves as a beacon of India's commitment to exploration, innovation, and self-reliance. The path ahead is both challenging and thrilling, with immense potential waiting to be harnessed. In the following paragraphs, we delve deeper into critical economic and policy imperatives and recommendations that could propel India's space industry to even greater heights.

[1] https://www.fortuneindia.com/macro/62-jump-in-funding-to-space-tech-startups-in-2023/114593#:~:text=Market%20intelligen ce%20 platform%20Tracxn%20notes,the%20same%20period%20last%20year

[2] https://economictimes.indiatimes.com/news/science/indias-space-economy-has-potential-to-reach-usd-44-bn-by-2033-says-top-official/ articleshow/104309396.cms

Expectations

Top asks

- While the India Space Policy, 2023 communicated the government's vision for the sector, the industry feels that the possibility of a policy being non-justiciable in a court of law does not augur well for the sector. This is because challenges around international and national obligations and liabilities, and enforcement of standards can be conclusively answered only in the form of a legislation. Hence, the early enactment of the much-anticipated Space Activities Act may be optimal for the ecosystem.
- The industry widely acknowledged GST exemption provided on satellite launch services.[3] However, for the benefit of the sector's value chain, the exemption can be extended to other critical components of satellites, ground systems, and launch vehicles. Further, while such exemption reduces GST cost on output activity of satellite launch services, the resultant impact on the input tax credit on procurement of goods and services should also be analysed. This adds to the cost of providing service. Thus, similar exemption should be provided for the procurement of key goods and services (including capital goods) by business for the purpose of satellite launch services. This will help reduce the GST input tax credit costs and the intended benefit would be enjoyed by the supply chain.
- As space industrial parks planned to be developed in various states, several non-government entities (legacy + start-ups) plan to make large greenfield investments. Therefore, we must consider other initiatives, such as tax exemptions/tax holidays/accelerated depreciation for companies directly or indirectly engaged in space sector activities. Further, specific customs duty exemption and concessions on import of goods/equipment/machinery used to manufacture notified goods under the Import of Goods at Concessional Rate of Duty scheme (IGCR) should be considered for the sector.
- The space industry necessitates substantial funding for capital-intensive projects, such as research and development, satellite manufacturing, and the construction of satellite launch and earth stations. Reducing tax rate on interest on foreign borrowings to 5 percent could catalyse Indian companies to access foreign funding at cost-effective interest rates for project financing.
- The withholding tax rate applied to payments made to Indian companies providing satellite services is currently set at 10 percent under section 194J of the Income-tax Act, 1961. However, the effective income-tax rate on revenue for service providers operating under a distribution model, where they distribute satellite capacity in India, is considerably lower than 10 percent. This is primarily due to the arm's length profit margin for Indian companies typically falling within the range of 5–10 percent. Even in case of service providers offering services through their own or leased satellites, the initial period witnesses a lower effective income-tax rate on revenue. To ensure that funds are not tied up to enable a seamless working capital flow, the withholding tax rate should be reduced to 2 percent on payments made to Indian companies.
- As self-reliance has been one of the key objectives behind opening the sector for private participation, ensuring journey towards self-reliance is focused on each value chain segment, is important. To that extent, it may be time to consider a dedicated Production Linked Incentive (PLI) scheme to manufacture space-grade components much like the recently announced dedicated PLI scheme for drones and drones' components.[4] This will help incentivise domestic production under the "Make in India" campaign and attract investment by providing financial incentives to manufacturers based on their output.
- Even in the NewSpace era where private-sector efforts will complement national space agencies and public-sector efforts, the nature of space-based applications and services makes governments a critical consumer/customer to the sector. As space technologies find applications in governance areas, such as agriculture, disaster management, infrastructure planning and development monitoring, urban development, and remote area connectivity, the government's commitment to adopt and consume NewSpace solutions will catalyse adoption and innovation in the sector.
- In line with the above, a Digital Public Infrastructure (DPI) and Digital Public Goods (DPG) approach for Earth observation-based geospatial analytics and insights can unlock value and innovation to several stakeholders well beyond the space sector. In line with previous budget announcements to create DPI for sectors, including agriculture, a budget announcement for a DPI/DPG for earth observation will pave the way for democratisation of access to space technology.

[3] https://www.businesstoday.in/latest/in-focus/story/gst-exemption-to-private-satellite-launch-service-firms-a-huge-financial-incentive-to-boost-growth-industry-389459-2023-07-12

[4] https://pib.gov.in/PressReleasePage.aspx?PRID=1913565#:~:text=For%20this%20scheme%2C%20the%20PLI,of%20drone%20and%20drone%20components.'s

- As the space sector matures, the space economy's size and composition should be regularly measured. Most of the mature space faring nations, such as the US, the UK, and EU, have annual exercises to scientifically measure and quantify the space economy. Annual exercise anchored by competent authority within the government to measure and disclose the size of the space economy, will enable quick and hassle-free investment decisions by the government, and private and international stakeholders.

Policy recommendations and expected impact

- The number of NewSpace start-ups registered in India has crossed 400.[5] With many of them keen to raise capital for growth, clarity of Foreign Direct Investment (FDI) for the sector will be beneficial. Apart from giving access to global capital, clarity on FDI through the much-awaited FDI policy for the sector will also reduce the cost of doing business for investors and companies.
- Provisioning of spectrum for several satellite applications viz., remote sensing, communications is mission critical for the sector. With Indian enterprises gearing up to meet global demands, adherence to global standards both nationally and internationally is important for innovating in India. Hence, a long-term commitment from the government on provisioning spectrum for satellite applications in India is needed. Sustained efforts at international forums to maintain global standards and a level-playing field for countries will be critical.
- Similar to the telecom sector, satellite service providers may be obligated to remit a one-time licence or spectrum fee to the government to secure the licence to deliver satellite services in India. Additionally, an annual licence fee is based on revenue may apply. At present, the provisions in place, as applicable to the telecom sector, allow for the amortisation of the one-time licence or spectrum fee over the typical licence duration that ranges from 10 to 20 years. With regard to the deduction of the annual license fee based on revenue, a legal precedent set by the Supreme Court deems this expenditure akin to a one-time fee and mandates its amortization over the remaining licence period. This treatment of delayed deduction of costs has led to increased tax liabilities. For the satellite sector, a more equitable approach would involve permitting a 25 percent depreciation. This is in line with intangible assets on the one-time licence or spectrum fee, while recognising the annual licence fee paid based on revenue as revenue expenditure. The depreciation could yield lower taxable profits for satellite service providers, resulting in optimising tax impact and providing economic impetus to business operations.

[3] https://www.thehindu.com/business/india-space-start-ups-say-funding-remains-biggest-challenge/article67307862.ece

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