Introduction and budget summary

The Finance Minister ('FM') presented the 2021 Union budget proposals before the Parliament on February 1, 2021.

Some of the key proposals included increased budget allocation to the health sector, privatisation of public sector undertakings and increase in permissible FDI norms for the insurance sector.

While the FM has not proposed any change to the tax slab rates, she has proposed to widen the scope of tax withholding as well as tax collection. The ongoing objective of the current Government to 'tax the rich' continues to display in these proposals.

In the following paragraphs, we have summarised the key direct tax proposals impacting the global mobility space.

Key budget proposals

- Taxation of Unit Linked Insurance Policy schemes

  Presently, proceeds on maturity of a Unit Linked Insurance Policy ('ULIP') are exempt from tax subject to satisfaction of certain conditions. There are no monetary limits prescribed to the amount of exemption a taxpayer can claim and this makes ULIPs a favourable and preferred investment scheme for taxpayers.

  The FM has proposed to limit the available exemption only to those cases where the aggregate annual premium payable for all policies held by a taxpayer, does not exceed Rs 250,000. The FM has proposed to grandfather policies issued prior to February 1, 2021 and therefore, the cap will only apply to policies issued on or after February 1, 2021.

  The FM has also proposed that exemption capping will not apply to proceeds received in case of death of a policy holder.

  Since the premium cap is fairly low, this proposal will impact middle income and high-income class of taxpayers who relied on ULIPs to secure their future and earn tax free income.

- Taxability of specified Provident Fund interest

  Presently, interest income accrued to the balance of specified Provident Funds is exempt from tax subject to satisfaction of continuous employment conditions. There are no monetary limits prescribed to the amount of exemption a taxpayer can claim.

  The FM has now proposed to limit the exemption to interest payable on Provident Fund contributions upto Rs 250,000 per annum and tax the interest payable on any amount exceeding this cap. This amendment is proposed to take effect for contributions starting from April 1, 2021.

  The proposed amendment will impact high salary income earners who have large Provident Fund contributions from their salary.

- Rationalisation of timing mismatch of foreign retirement fund income

  Presently, taxpayers who trigger residency in India but have foreign retirement fund income face timing mismatch issues, both towards reporting of the income as well as claiming tax credit in India.

The FM has proposed to introduce a new section, with effect from April 1, 2022, to address this issue and eliminate hardship to taxpayers. The FM has announced that detailed rules towards this proposal will be notified in due course.

We expect the Government will try to match the timing of taxability of such foreign retirement fund income to that of the foreign country. However, it has been proposed that the new section will only be applicable to notified foreign retirement funds. Therefore, this proposal may not apply to all cases.

While we will have to wait for the notified rules to evaluate the impact, we do expect that this will bring relief to international travelers.

- <u>Advance tax on dividend income</u>

  Presently, advance tax is payable on dividend income and a taxpayer is required to estimate the entire year's dividend and pay taxes within prescribed instalments. This leads to cases where a taxpayer has to pay interest due to errors in estimation of dividend income.

  The FM has proposed that, with effect from tax year 2020-21, taxpayers would now be responsible for making advance tax payments only upon declaration or payment of dividend, as the case may be. The advance tax payment would need to be made on a catch-up basis within the timeline of the next instalment.

  This is a welcome proposal as this would ease advance tax payment on dividend income.

- <u>Higher withholding tax rate for non-filers of tax returns</u>

  Presently, specified payments attract withholding tax or collection of tax, regardless of the compliance status of the recipient.

  The FM has proposed that, with effect from July 1, 2021, where a recipient has not filed a tax return for the preceding two consecutive years, and their tax withholding or tax collection for such previous years exceeded an amount of Rs 50,000 per year, tax withholding or collection of tax would need to be done at a higher rate. It has been proposed that the withholding tax or tax collection rate would be twice the existing rate or 5 percent, whichever is higher.

  Certain payments, including salary, are proposed to be excluded from this higher rate.

  While this proposal aims at increasing tax compliance by income earners, it is bound to create hardship for payers as there would be administrative challenges in collecting and verifying data from the recipients. We will have to wait and see if the Government releases any further guidance or procedural rules on this proposal.

- <u>Tax withholding on purchase of goods</u>

  Presently, tax withholding is not required to be undertaken at the time of purchase or sale of goods.

  The FM has proposed to introduce a new section, with effect from July 1, 2021, where persons having an annual turnover exceeding Rs 100 million would be required to withhold taxes from payments to an Indian tax resident where the aggregate annual purchases from such resident exceed Rs 5 million.

This proposal would increase the administrative and compliance burden of impacted persons.

- <u>Definition of the term 'liable to tax'</u>

Presently, the term 'liable to tax' has not been defined and, at times, it leads to uncertainty in interpretation of the law, especially in the case of international tax treaties.

The FM has proposed to introduce a new section, with effect from April 1, 2020, to define this term to mean that a person will be treated as being liable to tax where there is a liability of tax on that person under the law of any country, and would also include cases where subsequent to the imposition of tax liability in that country, an exemption from tax has been provided.

This would have a far-reaching impact on taxpayers and would bring much needed clarity on interpretation of international tax treaties.

- <u>Miscellaneous proposals</u>

Cash in lieu of Leave Travel Concession ('LTC')

The FM has proposed that, in order to provide relief to salary income earners who have not been able to claim and exemption towards LTC, they would be allowed to claim a relief towards any amount spent by them between October 12, 2020 to March 31, 2021 on goods and services on which GST has been paid at 12 percent.

The maximum benefit allowed under this proposal would be Rs 36,000 or one-third of the amount of spent, whichever is lower.

Affordable housing

In order to boost the real estate sector, the FM has proposed to extend the additional relief of Rs 150,000 for home loans for affordable housing by a further period of one year to March 31, 2022.

Faceless scheme for Income Tax Appellate Tribunal ('ITAT')

The FM has proposed to extend the faceless scheme for disposal of appeals to the ITAT and that adequate rules and directions will be issued before March 31, 2023 to facilitate such faceless scheme.

Increase in threshold limit for tax audit

The FM has proposed, with effect from tax year 2020-21, to increase the threshold limit for tax audit from Rs 50 million to Rs 100 million in cases where at least 95 percent of the business receipts and payments are made through electronic modes.

Reduction in various compliance time limits

The FM has proposed, with effect from tax year 2020-21, to reduce the time limit for filing of belated return or revised return by taxpayers by a period of 3 months.

Correspondingly, the time limit for various timelines of the tax department like processing of Income tax returns, issuing audit notices and completion of such audits have also been reduced by a period of 3 months.

Reopening of cases

The FM has proposed, with effect from April 1, 2021, to reduce the time limit for reopening an assessment of a tax return from 6 years to 3 years. This would not include cases where the income escaping assessment exceeds or is likely to exceed Rs 5 million, in which case the notice would still be permitted to be issued within 10 years but with approval of the Chief Commissioner of Income tax.

Relief to Senior Citizens

The FM has proposed, with effect from April 1, 2021, to provide an exemption from tax return filing for resident senior citizens, aged 75 years or above, who only have pension and interest income.

Conclusion

The budget proposals will be ratified only after both the Houses of Parliament and the President give their assent.

However, they have been well received by the market and resulted in a strong growth spurt in the stock market. Compliance measures continue to be proposed with a focus on self-governance and reporting.

Clients should evaluate the impact of the proposals and plan their transactions and investments accordingly.

About us

Broadening Horizons is a specialty services company providing expatriate tax, social security, immigration and exchange control advisory and compliance services.

It has specially designed service packages for employers with cross-border employee population as well as individuals.

Broadening Horizons partners with international expatriate tax firms for delivering mobility services and therefore, can provide cross-border services and solutions.

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