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Understanding Important Amendments Made in the Finance Bill 2023 as passed by Lok Sabha



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With the second leg of the Budget Session getting affected by disruptions, the Finance Bill 2023 has been passed in the Lok Sabha on 24.3.2023, through the 'Guillotine' method under which all the Bills, grants and funds are passed by the Government without any debate.

Among the total 64 amendments made in the Finance Bill 2023, let us understand some of the important amendments, which stand out on account of their wide scale ramifications.

New Rules for Taxation of Debt Mutual Funds:

The first significant amendment is in respect of debt mutual funds. The initial Finance Bill 2023, has inserted a new section 50AA, providing for the taxability of any gain on transfer, redemption or maturity of the market linked debenture (MLD) on or after 1.4.2023, as a short-term capital gain, irrespective of the period of holding.

Now the coverage of this newly inserted section 50AA has been further expanded to include the units of specified mutual funds. The specified mutual fund has been defined as that mutual fund where not more than 35% of the total proceeds are invested in equity shares of domestic companies or in other words the debt mutual funds, acquired on or after 1.4.2023.

Thus, w.e.f. 1.4.2023, any gain or income arising on transfer, redemption or maturity of a unit of debt mutual funds, acquired on or after 1.4.2023, will be considered as short-term capital gain, and taxable at the applicable slab rate of the investor, irrespective of the period of holding. Indexation benefit is also not available in case of short-term capital gain.

It is interesting to note here that this amended tax treatment is also applicable on International Equity Funds, Exchange Traded Funds, Gold/Silver Exchange Traded Funds, Target Maturity Funds, Fund of Funds ETFs.

Presently, the units of debt mutual funds, held for more than three years are taxable as long-term capital

gains and are taxable @ 20% plus applicable surcharge and cess, along with the indexation benefit.

It appears that this amendment has been made to bridge the existing tax arbitrage between debt funds and bank fixed deposits/NPS/other insurance products, to make the latter instruments at par with the debt funds, from the taxation point of view, to the investors.

Thus, the Mutual Fund Houses may consider tweaking their investment portfolio to ensure a marginally more investments in equity funds than the threshold criteria of 35%, so as to do away with the denial of the benefit of taxability as long term capital gains and the indexation benefits. However, this will require the prior approval of SEBI, which in itself may not be an easy compliance. So, all in all, the mutual fund industry is bound to get adversely affected by this silent amendment in the Finance Bill 2023, brought about in serial nos. 20, 21, 22 & 23 in amendment schedule.

It will be interesting to see that whether the SVB crisis has anything to do with this amendment, so as to make the bank fixed deposits an attractive investment option and at par with the long-term debt funds, from the taxation point of view, to the investors, so as to prevent any unforceable bank run in India.

Marginal Relief found its way in the New Personal Tax Regime

The second significant amendment is in respect of provision of 'marginal relief' in the new personal tax regime. The marginal relief in respect of taxpayers, having their annual gross total incomes of Rs. 7,00,005 and upto Rs. 7,29,000/-, and opting for the new tax regime, has now been provided such that, at such income levels, the income tax payable will get restricted to the amount of income which exceeds Rs. 7,00,000 only, and not higher than that.

Relaxation on the Taxability of Debt Repayments by Business Trusts (REIT/InvIT) to the unit holders

The third important amendment is in respect of imparting further clarity and relaxation on the taxability of distributed incomes by business trusts (REIT/InvIT) to the unit holders.

The initial Finance Bill 2023 has inserted a new section [56\(2\)\(xii\)](#) to tax the distribution of the 'specified sum' in the form of interest, dividend and rental income and repayment of debt by the business trusts, to the unit holders, as income from other sources, at their respective slab rates.

Now, a specific formula has been prescribed to compute this 'specified sum', as under:

Specified sum = A-B-C,

Wherein,

A= Cumulative distributions made to the unit holders, other than distributions covered under the provisions of section [10\(23FC\)](#)/ [10\(23FCA\)](#) and not chargeable to tax under Section [115UA\(2\)](#)

B= Issue price

C= Amount already taxed in any of the previous year

Further, it has also been provided that if B+C is greater than A, then the specified sum will be NIL.

So, this amendment is a welcome relief for the unit holders of business trusts, as after this amendment, the

debt repayments by the business trusts shall not effectively come under the tax net as income from other sources, as these will get offset by the issue price. There shall be no tax on the amortisation of business trusts (SPV) debt till such time that the aggregate amount of amortisation of SPV debt does not exceed the issue price. Such repayments of debt shall get reduced from the cost of acquisition in the hands of unit holders of the business trusts. So, unit holders will pay the capital gains tax only when they eventually transfer their units in such business trusts on the difference between the sale consideration and the adjusted cost of their units in the business trusts i.e., original cost minus the debt repayments (amortised debts) received by the unit holders till the date of such transfer.

Therefore, after this welcome amendment, the debt repayments (amortisation of debt) shall get taxed under the head income from other sources, at the maximum marginal rate of tax only if they exceed the issue price of such units. However, as a revenue balancing measure, such debt repayment (amortisation of debt) shall get reduced from the cost of acquisition of such units of the business trusts in the hands of the unit holders.

Increase in Domestic Withholding Tax Rate on Royalty and Fees for Technical Services payments

Another significant amendment is the increase in the domestic withholding tax rate on royalty and fees for technical services payments by Indian taxpayers to non-resident entities from the existing 10% to 20% u/s [115A](#) of the Income Tax Act. This will now push such non-resident entities to pursue for treaty benefits of lower withholding tax rates, under Double Taxation Avoidance Agreements (DTAAS). The US, UK, Netherlands and many other Tax Treaties provide for a lower withholding tax rate of 10% or 15% on such royalty and FTS payments and also provide the benefit of 'make available clause' in respect of technical services.

However, the procedural requirement of filing Form 10F as stipulated by section [90\(4\)](#) in addition to the tax residency certificate (TRC) may create some ground-level practical difficulties for such enterprises, in the absence of PAN.

It needs to be understood and appreciated here that in majority of such contracts, the liability of withholding tax is to be borne by the Indian counter party only and not the non resident entity and grossing up of the withholding tax is being done. So, now this further increase in the domestic withholding tax rate on FTS and royalty payments from the existing 10% to 20%, will actually lead to a substantial increase in the technology related costs of the Indian enterprises, engaged in the technology and research and development sector.

CBDT has provided a one-time relaxation to such non resident entities by allowing the manual filings of the said Form 10F uptill 31.3.2023, without having the requirement to register online on the Income Tax portal, for which PAN is compulsorily needed. However, such a brief relaxation window, may not be sufficient to address the genuine ground-level difficulties

Credit Card Payments towards Foreign Tours Made Subject to TCS

Among the ruckus in the Lok Sabha, the hon'ble FM has briefly clarified that the Reserve Bank of India has been advised to ensure that the Credit Card payments towards foreign tours are brought under the purview of Liberalised Remittances Scheme (LRS) and are also made subject to the levy of Tax Collected at Source (TCS) @ 20%.

Constitution of GST Appellate Tribunals

In the Indirect Tax front, enabling provisions have been provided for the Constitution of GST Appellate Tribunals with establishment of the principal bench in New Delhi and various State benches in various States.

Parting Thought: For ensuring healthy discussion and awareness of all the stakeholders involved including the taxpayers, whom our hon'ble Prime Minister Shri Narendra Modi ji has referred to as the 'Wealth Creators' of the Nation, it is imperative and desirable that the above 64 amendments should have been brought out in the original version of the Finance Bill 2023 only, at the time of its presentation in the Parliament on 1.2.2023.

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