A COMPLETE ANALYSIS OF THE FINANCE ACT, 2013
PART - II
(Chapter IV of the IT Act)

Prepared by Advocates of
M/s Subbaraya Aiyar, Padmanabhan & Ramamani (SAPR) Advocates

3. CHAPTER IV – Computation of Total Income

Profit and gains of business or profession

a. Section 32AC: Investment allowance

Amendment:

After section 32AB of the Income-tax Act, the following section shall be inserted with effect from the 1st day of April, 2014, namely:—

'32AC. (1) Where an assessee, being a company, engaged in the business of manufacture or production of any article or thing, acquires and installs new asset after the 31st day of March, 2013 but before the 1st day of April, 2015 and the aggregate amount of actual cost of such new assets exceeds one hundred crore rupees, then, there shall be allowed a deduction,—

(a) for the assessment year commencing on the 1st day of April, 2014, of a sum equal to fifteen per cent. of the actual cost of new assets acquired and installed after the 31st day of March, 2013 but before the 1st day of April, 2014, if the aggregate amount of actual cost of such new assets exceeds one hundred crore rupees; and

(b) for the assessment year commencing on the 1st day of April, 2015, of a sum equal to fifteen per cent. of the actual cost of new assets acquired and installed after the 31st day of March, 2013 but before the 1st day of April, 2015, as reduced by the amount of deduction allowed, if any, under clause (a).

(2) If any new asset acquired and installed by the assessee is sold or otherwise transferred, except in connection with the amalgamation or demerger, within a period of five years from the date of its installation, the amount of deduction allowed under sub-section (1) in respect of such new asset shall be deemed to be the income of the

assessee chargeable under the head “Profits and gains of business or profession” of the previous year in which such new asset is sold or otherwise transferred, in addition to taxability of gains, arising on account of transfer of such new asset.

(3) Where the new asset is sold or otherwise transferred in connection with the amalgamation or demerger within a period of five years from the date of its installation, the provisions of sub-section (2) shall apply to the amalgamated company or the resulting company, as the case may be, as they would have applied to the amalgamating company or the demerged company.

(4) For the purposes of this section, “new asset” means any new plant or machinery (other than ship or aircraft) but does not include—

(i) any plant or machinery which before its installation by the assessee was used either within or outside India by any other person;

(ii) any plant or machinery installed in any office premises or any residential accommodation, including accommodation in the nature of a guest house;

(iii) any office appliances including computers or computer software;

(iv) any vehicle; or

(v) any plant or machinery, the whole of the actual cost of which is allowed as deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head “Profits and gains of business or profession” of any previous year.’.

Analysis:

Every proposed Finance bill or a Finance Act is passed with the following two important objectives:

- To increase the tax base and
- To stimulate Socio-Economic growth

These two objectives can be combined to form a quintessential Budget. In other words, these two objectives represent two sides of a coin and as such it may lead to adverse consequences at the macro level if they were not blended properly such as a) erosion of tax base, b) over incentivizing a particular sector may prove detrimental to other sectors, etc.

Following are the ways through which the government tends to stimulate the socio-economic growth:

a) By providing excess depreciation or investment allowance or weighted deduction etc.
b) By allowing to establish the tax free enterprise in the Special Economic Zones such as 10A unit or 10B unit etc.
c) By providing excess deductions to *eligible business unit* such as 80IA units, etc

These can also be called as **'Tax Incentives'**. These incentives are designed to develop the economically lagging enterprises and industries.

The proposed Finance Bill, 2013 though did not give us as many surprises as the previous Finance Bill but did very little to change the perspective of investors towards Indian Economy, more particularly, Indian tax laws.

Finance Bill, 2013 has very few meaningful tax incentives, one of which is *Investment allowance u/s 32AC.*

Investment Allowance:

Investment allowance is basically provided to promote capital expansions or to boost the economically lagging industries. One of the highlights of the Finance Bill, 2013 is that it did not restrict the Investment Allowance to any particular industry but has extended it to all manufacturing companies.

Section 32AC:

Under the proposed Bill, any manufacturing company which installs new asset after 31st March, 2013 but before 1st April, 2015 and if the aggregate cost of the new asset exceeds 100 crores of rupees then the aforementioned manufacturing company shall be entitled to a deduction of 15% of the actual cost of the new asset for the first year i.e. AY 2014-15 and a further deduction of 15% on the cost of the new asset as reduced by the deduction earned in the previous year in the second assessment year i.e., AY 2015-16.

However, if the new asset (worth more than 100 crores) is installed after 31st March, 2014 but before 1st April, 2015 the assessee will not be eligible for deduction for 2 years but for only one year as the Investment Allowance period ends by the AY 2015-16.

Precautionary clause:

In order to overcome the mal-usage of the Section, the proposed Finance Bill has inserted a precautionary clause which mandates the assessee to own the newly acquired the asset for a period of at least five years. The amount given as deductions under this section will be included in the total income of the assessee in the financial year in which the assessee sells the newly acquired asset irrespective of the taxation of the capital gains generated on the sale.

However, this restriction shall not apply to the amalgamated or resulting company in a scheme of amalgamation.

Comments:

Although it is a positive step on the part of the government to provide incentives to the manufacturing industries, the prescribed minimum limit of 100 crores is quite high and as such no industry may be ready to invest over 100 cores to acquire a capital asset in order to avail the deduction of 15% for 2 years. It is only those assessee who have already started installing the new asset may be availing this benefit.

Bringing down the minimum ceiling limit to 10 or 20 crores would definitely help to boost the small and medium scale industries.

[SECTION 6 OF THE FINANCE ACT, 2013]

b. Section 36: Other deductions

Amendment:

In section 36 of the Income-tax Act, in sub-section (1), with effect from the 1st day of April, 2014,—

(a) in clause (vii), the Explanation shall be numbered as Explanation 1 thereof and after Explanation1 as so numbered, the following Explanation shall be inserted, namely:—

“Explanation 2.—For the removal of doubts, it is hereby clarified that for the purposes of the proviso to clause (vii) of this sub-section and clause (v) of sub-section (2), the account referred to therein shall be only one account in respect of provision for bad and doubtful debts under clause (viia) and such account shall relate to all types of advances, including advances made by rural branches;”

(b) after clause (xv), the following clause shall be inserted, namely:—

‘(xvi) an amount equal to the commodities transaction tax paid by the assessee in respect of the taxable commodities transactions entered into in the course of his business during the previous year, if the income arising from such taxable commodities transactions is included in the income computed under the head “Profits and gains of business or profession” assigned to them under Chapter VII of the Finance Act, 2013.’.

Explanation.—For the purposes of this clause, the expressions “commodities transaction tax” and “taxable commodities transaction” shall have the meanings respectively assigned to them under Chapter VII of the Finance Act, 2013.’.

Analysis:

a) **Section 36 (1) (viia):** Clarification for amount to be eligible for deduction as bad debts in case of banks

The amendment to this section seeks to clarify the amount to be eligible for deduction as bad debts in case of banks. The need for clarification arises from the various judicial pronouncements which has created doubts about the about the scope and applicability of proviso to section 36(1)(vii). The rulings in the following cases have created a sense of ambiguity in the interpretation of this provision.

(1) In the case of **DCIT v. Karnataka Bank Ltd. [2012] 25 taxmann.com 235***,* the Supreme Court held that in case of scheduled bank, deduction under section 36(1)(vii) is allowable independently and irrespective of provision for bad and doubtful debts created by it in relation to advances made by its rural branches, provided the amount is not deducted twice under section 36(1)(vii) and 36(1)(viia) simultaneously.

(2) In the case of **Catholic Syrian Bank Ltd. v. CIT [2012] 18 taxmann.com 282**, the Supreme Court laid down following principles with regard to deduction for bad debts:

(a) Provisions of sections 36(1)(vii) and 36(1)(viia) are distinct and independent items of deduction and operate in their respective fields.

(b) If amount of bad debt actually written off in accounts of bank represents only debt arising out of urban advances, allowance thereof in assessment is not affected, controlled or limited in any way by provisions of Section 36(1)(vii).

(3) In the case of **CIT. v. South Indian Banks Ltd. [2010] 191 Taxman 272 (Ker),**the High Court held that for application of ceiling provided in Sec. 36(1)(vii), Legislature does not make any distinction between provision created in respect of advances made by rural branches of bank and advances made by other branches of bank.

Hence by the amendment, it becomes clear that, in case of banks and financial institutions, to which section 36(1)(viia) applies, the amount of deduction in respect of the bad debts actually written off under section 36(1)(vii) shall be limited to the amount by which such bad debts exceeds the credit balance in the provision for bad and doubtful debts account created under section 36(1)(viia) without any distinction between rural advances and other advances.

This amendment will take effect from 1st April, 2014 and will, accordingly, apply in relation to the assessment year 2014-15 and subsequent assessment years.

b) **Section 36 (1) (xvi):** Commodities Transaction Tax

The Chapter VII to Finance Bill, 2013 seeks to introduce Commodities Transaction Tax in a limited way and is applicable for those dealing in trading of commodities. While agricultural commodities will be exempted from CTT, non-farm commodities like gold, silver and non-ferrous metals such as copper and energy products like crude oil and natural gas will be taxed. The Finance Bill, 2013, seeks to impose CTT at the rate of 0.01% on the sale of derivate commodity which shall be payable by the seller.

In consonance to the introduction of CTT, an amendment to section 36 has been proposed. A new provision, clause (xvi) has been inserted to provide that an amount equal to the commodities transaction tax paid by the assessee in respect of the taxable commodities transactions entered into in the course of his business during the previous year shall be allowable as deduction, if the income arising from such taxable commodities transactions is included in the income computed under the head “Profits and gains of business or profession.

This amendment in section 36 of the Income-tax Act will take effect from 1st April, 2014 and will, accordingly, apply in relation to the assessment year 2014-15 and subsequent assessment years.

[SECTION 7 OF THE FINANCE ACT, 2013]

c. Section 40: Disallowance of deduction to State Government undertakings on any payment made by it to the State Government

Amendment:

In section 40 of the Income-tax Act, in clause (a), after sub-clause (iia), the following sub-clause shall be inserted with effect from the 1st day of April, 2014, namely:—

"(iib) any amount—

(A) paid by way of royalty, licence fee, service fee, privilege fee, service charge or any other fee or charge, by whatever name called, which is levied exclusively on; or

(B) which is appropriated, directly or indirectly, from, a State Government undertaking by the State Government.

Explanation.—For the purposes of this sub-clause, a State Government undertaking includes—
(i) a corporation established by or under any Act of the State Government;
(ii) a company in which more than fifty per cent. of the paid-up equity share capital is held by the State Government;
(iii) a company in which more than fifty per cent. of the paid-up equity share capital is held by the entity referred to in clause (i) or clause (ii) (whether singly or taken together);
(iv) a company or corporation in which the State Government has the right to appoint the majority of the directors or to control the management or policy decisions, directly or indirectly, including by virtue of its shareholding or management rights or shareholders agreements or voting agreements or in any other manner;
(v) an authority, a board or an institution or a body established or constituted by or under any Act of the State Government or owned or controlled by the State Government;".

Analysis:

Any payment by way of royalty, licence fee, privilege fee or any other fee, which is levied exclusively on or appropriated directly or indirectly from the State Government, shall not be deducted in computing the income chargeable under the head "Profits and Gains of business or profession."

[SECTION 8 OF THE FINANCE ACT, 2013]

d. Section 43: Definitions of certain terms relevant to income from profits and gains of business or profession.

Amendment:

(I) The proviso to Section 43(5) has been amended by the ***Finance Act 2013*** *to insert the following proviso:*

(A) in clause (d), after the words "a recognised stock exchange;", the word "or" shall be inserted;

(B) after clause (d), the following clause shall be inserted, namely:—

"(e) an eligible transaction in respect of trading in commodity derivatives carried out in a recognised association,";

(II) The Explanation shall be numbered as "Explanation 1" thereof and in the Explanation 1 as so renumbered, for the words "this clause", the word, brackets and letter "clause (d)" shall be substituted

(III) After Explanation 1 as so renumbered, the following Explanation shall be inserted, namely:

'Explanation 2 : For the purposes of clause (e), the expressions—

(i) "commodity derivative" shall have the meaning as assigned to it in Chapter VII of the Finance Act, 2013;

(ii) "eligible transaction" means any transaction,—

(A) carried out electronically on screen-based systems through member or an intermediary, registered under the bye-laws, rules and regulations of the recognised association for trading in commodity derivative in accordance with the provisions of the

Forward Contracts (Regulation) Act, 1952 (74 of 1952) and the rules, regulations or bye-laws made or directions issued under that Act on a recognised association; and

(B) which is supported by a time stamped contract note issued by such member or intermediary to every client indicating in the contract note, the unique client identity number allotted under the Act, rules, regulations or bye-laws referred to in sub-clause (A), unique trade number and permanent account number allotted under this Act;

(iii) "recognised association" means a recognised association as referred to in clause

(j) of section 2 of the Forward Contracts (Regulation) Act, 1952 (74 of 1952) and which fulfils such conditions as may be prescribed and is notified by the Central Government for this purpose."

Analysis:

The scope of transactions to be excluded from the scope of speculative transactions under section 43(5) of the Act has been extended to transactions in commodity derivatives carried out in a recognised association.

The terms 'eligible transaction', 'recognised stock exchange' and 'recognised association' and 'commodity derivative' have been defined for the purposes of this section.

[SECTION 9 OF THE FINANCE ACT, 2013]

e. Section 43CA: Full value of consideration for transfer of assets other than capital assets

Amendment:

After section 43C of the Income-tax Act, the following section shall be inserted with effect from the1st day of April, 2014, namely:—

"43CA. (1) Where the consideration received or accruing as a result of the transfer by an assessee of an asset (other than a capital asset), being land or building or both, is less than the value adopted or assessed or assessable by any authority of a State Government for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed or assessable shall, for the purposes of computing profits

and gains from transfer of such asset, be deemed to be the full value of the consideration received or accruing as a result of such transfer.

(2) The provisions of sub-section (2) and sub-section (3) of section 50C shall, so far as may be, apply in relation to determination of the value adopted or assessed or assessable under sub-section (1).

(3) Where the date of agreement fixing the value of consideration for transfer of the asset and the date of registration of such transfer of asset are not the same, the value referred to in sub-section (1) may be taken as the value assessable by any authority of a State Government for the purpose of payment of stamp duty in respect of such transfer on the date of the agreement.

(4) The provisions of sub-section (3) shall apply only in a case where the amount of consideration or a part thereof has been received by any mode other than cash on or before the date of agreement for transfer of the asset.".

Analysis:

Clause 8 seeks to insert Sec 43CA to provide for a special provision for taxation of the full value of consideration for transfer of assets other than capital assets in certain cases, with effect from Assessment Year 2014-15.

The Finance Bill 2013 proposes to introduce a new provision similar to Section 50C of the IT Act. The proposed section provides that where the consideration for the transfer of an asset (other than capital asset), being land or building or both, is less than the stamp duty value, stamp duty value shall be deemed to be the full value of consideration for the purposes of computing income under the head 'Profits and gains of business of profession' (PGBP)

While Sec 50C makes a provision for full value of consideration in respect of transfer by an assessee of a capital asset, the proposed Sec 43CA makes a provision for full value of consideration in respect of transfer by an assessee of an asset other than a capital asset and seeks to bring it under the head "business income".

The proposed sub section (1) seeks to provide that where the consideration received or accruing as a result of the transfer by an assessee of an asset (other than a capital asset), being land or building or both, is less than the value adopted or assessed or assessable by any authority of a State Government for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed or assessable shall be deemed to be the full value of the consideration received or accruing as a result of such transfer for the purposes of computing profits and gains from transfer of such asset. The provision of sub-section (2) and sub-section (3) of Section 50C in relation to the reference made to valuation officer are also proposed to be made applicable.

However, where:

- the date of agreement fixing the consideration and the date of registration are not the same; and
- the consideration or a part thereof has been received by any mode other than cash on or before the date of agreement fixing the consideration,

then the value referred to in sub-sec (1) may be taken as the value assessable by any authority of a State Government for the purpose of payment of stamp duty in respect of such transfer on the date of the agreement.

If this section is inserted, the following decisions will be nullified:

- The decision that the Provisions of section 50C will be applicable only to find out the true value of a capital asset and not for computing business income as held in **CIT Vs. Thiruvengadam Investments (P) Ltd 229 CTR 284 (Mad)** will no longer be applicable. In this case, Sec 50C was held not applicable as the property was treated as a business asset , i.e. **Section 50C would apply only to capital gains and not to business income, for example, assets held as stock in trade**
- In **M/s. Inderlok Hotels Pvt. Ltd. Vs. ITO [122 TTJ 145]**, the Tribunal held that Sec 50C cannot be applied for determining income under other heads.
- In **CIT VS M/S Kan Construction And Colonizers Pvt Ltd 012-TIOL-286-HC** held:Section 50C uses the word “capital asset.” Stock in trade has been excluded from the definition of capital asset. Section 50C has no application in a case of transfer of plots held as stock in trade.

Cases referred:

1. CIT Vs. Thiruvengadam Investments (P) Ltd 229 CTR 284 (Mad)

Provisions of s. 50C can be applied only to find out the true value of a capital asset and not for computing business income and, therefore, the same were not applicable in the matter of computation of assessee’s income from the sale of the property which was treated as business asset and not as capital asset in the hands of the assessee.

2. M/s. Inderlok Hotels Pvt. Ltd. Vs. ITO [122 TTJ 145]

Section 50C has application only to the extent of determining sale consideration for computation of capital gain under chapter IV-E of the Act and it cannot be applied for determining the income under other heads

3. CIT Vs. M/S Kan Construction And Colonizers Pvt Ltd 012-TIOL-286-HC

The provisions of section 50C are not applicable with respect of sale of land as sale of land was not capital asset.

[SECTION 10 OF THE FINANCE ACT, 2013]

Income from other sources

f. Section 56 (2): Taxability of income in respect of immovable property received for inadequate consideration

Amendment:

In section 56 of the Income-tax Act, in sub-section (2),—

(I) in clause (vii), for sub-clause (b), the following sub-clause shall be substituted with effect from the 1st day of April, 2014, namely:—

"(b) any immovable property,—

(i) without consideration, the stamp duty value of which exceeds fifty thousand rupees, the 5stamp duty value of such property;

(ii) for a consideration which is less than the stamp duty value of the property by an amount exceeding fifty thousand rupees, the stamp duty value of such property as exceeds such consideration:

Provided that where the date of the agreement fixing the amount of consideration for the 10 transfer of immovable property and the date of registration are not the same, the stamp duty value on the date of the agreement may be taken for the purposes of this sub-clause:

Provided further that the said proviso shall apply only in a case where the amount of consideration referred to therein, or a part thereof, has been paid by any mode other than cash on or before the date of the agreement for the transfer of such immovable property;";

(II) in clause (viib), in the Explanation, in clause (b), for the word and figure "Explanation 1", the word "Explanation" shall be substituted.

Analysis:

The Finance Bill 2013 proposes to amend section 56(2)(vii)(b) of the IT Act. The amendment provides that where any immovable property is received by an individual or HUF for consideration which is less than the stamp duty value of the property by an amount exceeding Rs. 50,000/-, the stamp duty value of such property as exceeding the amount of consideration shall be taxable as income from other sources.

Where there is a time gap between date of agreement and date of registration, the stamp duty value on the date of agreement may be considered. However, this will be applicable only when the consideration has been paid otherwise than by cash on or before the date of agreement fixing the consideration.

The proposed amendment will take effect from AY 2014-15 (FY 2013-14).

The proposed section 56(2)(vii) read with section 43CA/50C results in taxation at both the ends of the transaction where transfer/sale of immovable property takes place at a value less than the stamp duty value. While seller will be charged to tax either under the head capital gains or profits and gains on business and profession tax on sale/transfer, the buyer would have to pay tax as income from other sources on the differential amount.

[SECTION 11 OF THE FINANCE ACT, 2013]