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Impact Analysis of Reduction in Corporate Tax Rates

Analysis By Ved Jain



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Message

In its continuing endeavor to provide the requisite momentum to the growth process and create an enabling business environment, the Union Finance Minister on Friday, September 20, announced major reforms in the corporate tax structure of the country. With these changes, India has become very competitive and even better than other countries in the South East Asian region.

We feel that these are steps in the right direction and enable India to achieve its vision of becoming a \$5 trillion economy by 2024.

In this document, we present an in-depth analysis of the measures announced and their likely impact.

We hope that you will find this useful.

A handwritten signature in black ink, appearing to read 'Ved Jain'.

Ved Jain

Impact Analysis of Reduction in Corporate Tax Rates

The Hon'ble Finance Minister announced substantial reduction in the tax rates applicable to Domestic Companies. Post announcement by the Finance Minister, the Government of India has issued the Taxation Laws (Amendment) Ordinance, 2019 proposing various amendments in the Income Tax Act, 1961 as well as the Finance (No.2) Act, 2019. These reduction in tax rates will go a long way in attracting various multinational companies to shift manufacturing base in India. India will now be able to take advantage of the global trade issues and promote itself as manufacturing capital of the World. The effective tax rate of 17.16% for manufacturing companies is quite competitive or even better than the other competing economies of the South East Asia such as China, Thailand, Indonesia, Vietnam, Singapore, Hong Kong etc. The growth in economy and the job creation due to this will be far more beneficial as compared to any Revenue which is being forgone by this reduction in the tax rate. This Ordinance has 8 clauses. The amendments made by this Ordinance are analysed below. All the amendments are to be effective from 1st April, 2020 i.e. assessment year 2020-21 relating to income earned in financial year 2019-20 i.e. the year starting from 1st April 2019.

A. NEW CORPORATE TAX RATES VIS-A-VIS EXISTING RATES

1. CONCESSIONAL TAX RATE OF 22% TO APPLY TO DOMESTIC COMPANIES

The Taxation Laws (Amendment) Ordinance, 2019 has inserted a new section 115BAA in the Income Tax Act, to provide an option to all domestic companies to pay tax at concessional rate of 22 percent with fixed surcharge of 10 per cent and health and education cess of 4 percent. Thus, the effective tax rate for domestic companies will be 25.17 per cent.

There is no condition/limitation on account of turnover, whether such company is engaged in manufacturing or not, the type of business or activity of the company or the date when the company was incorporated. Thus, all existing as well new domestic companies are eligible to avail this concessional rate of tax. Further, it is to be noted that this provision is applicable to domestic companies which means Indian company i.e. all companies formed and registered in India including by Multinational Companies but does not include branch or permanent establishment of foreign companies. Tax rates in respect of other entities such as partnership firm, LLP, Individuals, HUF, etc. shall continue to be as notified in the Finance (No. 2) Act, 2019

2. COMPARISON OF RATES IN FORCE PRIOR TO THE ORDINANCE

Prior to insertion of above section 115BAA, there are existing broadly two tax brackets that were applicable in respect a domestic company i.e. 25 per cent and 30 per cent. Companies whose turnover in previous year 2017-18 did not exceed Rs. 400 crores were liable to pay tax at 25 per cent plus surcharge and health and education cess as applicable. Domestic companies whose turnover exceeded Rs. 400 crores in previous year 2017-18 were liable to pay tax at 30 per cent plus surcharge and health and education cess as applicable.

Further, there is another section 115BA that provide an option to pay tax at concessional rate of 25 per cent to domestic companies set up and registered on or after 31st march 2016 that are engaged solely 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. Under this provision, option to pay concessional rate of tax of 25 percent is available irrespective of the turnover of the company but with the condition that such company will not claim any deduction/exemption on account of SEZ under section 10AA, additional initial depreciation allowable at the rate of 20 per cent under section 32(1)(iia), investment allowance in respect of new plant and machinery under section 32AC, 32AD, Tea Development Benefit under section 33AB, Site Restoration benefit under section 33ABA, Scientific Research benefit under section 35, Social Welfare project benefit under section 35AC, 35AD, agricultural extension project benefit under section 35CCC, skill development project under section 35CCD, accelerated capital deduction for specified business under section 35AD, agricultural extension project benefit under section 35CCC, skill development project under section 35CCD and the benefit available under provisions of Chapter VI-A under the heading "C-Deductions in respect of certain incomes" i.e. 80IA, 80IB, 80IC, etc. other than section 80JJAA in respect of employment. While such option was available to the above said manufacturing companies irrespective of their turnover, such option was not available to the said company if it was incorporated prior to 31st march 2016.

The effective tax rates applicable prior to insertion of this new section 115BAA by the Ordinance can be summarized as under:

Income	Concessional tax rate for certain manufacturing domestic companies (Sec 115BA) without benefit of any exemptions/incentive		Domestic Companies whose turnover in Previous Year 2017-18 does not exceed Rs. 400 crores with benefit of exemptions/incentive		Domestic Companies whose turnover in Previous Year 2017-18 exceeds Rs. 400 crores with benefit of exemptions/incentive	
	Surcharge	Effective tax rate*	Surcharge	Effective tax rate*	Surcharge	Effective tax rate*
	Base tax rate: 25%		Base tax rate: 25%		Base tax rate: 30%	
Upto Rs. 1 crore	0%	26.00%	0%	26.00%	0%	31.20%
More than Rs. 1 crore but upto Rs. 10 crores	7%	27.82%	7%	27.82%	7%	33.38%
More than Rs. 10 crores	12%	29.12%	12%	29.12%	12%	34.94%

* Effective tax rates are inclusive of surcharge, wherever applicable and health and education cess @ 4%

3. TAX RATES COMPARISON AFTER INSERTION OF NEW SECTION 115BAA

Now, after the introduction of section 115BAA in the Act by this Ordinance, all domestic companies have been given an option to pay tax at concessional rate of 22 per cent but with a flat surcharge of 10 percent irrespective of the amount of income of such company. Further, health and education cess at the rate of 4 per cent will also be applicable on such tax and surcharge. Thus, the effective tax rate under this section 115BAA will be 25.17 per cent without benefit of any exemption/incentive.

Thus, the benefit to the companies whose turnover does not exceed Rs. 400 crores in previous year 2017-18 will only be of 0.83 per cent in case where income of such company does not exceed Rs. 1 crores. In the case of such companies where income exceeds Rs. 1 crore but does not exceed Rs. 10 crore, the benefit will only be 2.65 per cent. In the case of companies whose turnover exceeds Rs. 10 crores, the benefit will be of 3.95 per cent as is evident from the below table and that too after sacrificing benefit of various exemption/incentive as stated herein below, if any available to such companies:

Category of taxpayers	Domestic Companies whose turnover in Previous Year 2017-18 does not exceed Rs. 400 crores		
	Tax liability under normal provisions	Tax liability under section 115BAA	Net saving in taxes (in %)
Income Upto Rs. 1 crore	26.00%	25.17%	0.83%
Income more than Rs. 1 crore but upto Rs. 10 crores	27.82%	25.17%	2.65%
Income more than Rs. 10 crores	29.12%	25.17%	3.95%

These companies constitute 99.3 per cent of the total companies.

The real gainers of new provision introduced by this Ordinance will be the companies whose turnover exceeded Rs. 400 crores in previous year 2017-18 i.e. the remaining 0.7 per cent companies as can be seen from the following table:

Category of taxpayers	Domestic Companies whose turnover in Previous Year 2017-18 exceeds Rs. 400 crores		
	Tax liability under normal provisions	Tax liability under section 115BAA	Net saving in taxes (in %)
Income Upto Rs. 1 crore	31.20%	25.17%	6.03%
Income more than Rs. 1 crore but upto Rs. 10 crores	33.38%	25.17%	8.21%
Income more than Rs. 10 crores	34.94%	25.17%	9.77%

As per the above table, such companies will enjoy saving in taxes to the tune of 6.03 per cent in case its income does not exceed Rs. 1 crores, 8.21 per cent in case its income exceeds Rs. 1 crores but does not exceed Rs. 10 crores and 9.77 per cent in case its income exceeds Rs. 10 crores. Thus, the biggest gainer with this amendment will be companies having turnover of more than Rs. 400 crores and income above Rs. 10 crores. Such companies will save 9.77 per cent which means saving of about 28 per cent ($9.77/34.94 \times 100$) of present tax liability.

4. DEDUCTIONS/INCENTIVES TO BE FORGONE IN CASE COMPANY OPTS TO PAY TAX AT CONCESSIONAL RATE UNDER SECTION 115BAA

Apparently, the benefit of concessional tax under new section 115BAA is impressive. However, it is to be noted that such companies while computing the total income have to forego deduction on account of SEZ under section 10AA, additional initial depreciation allowable at the rate of 20 per cent under section 32(1)(iia), investment allowance in respect of new plant and machinery under section 32AC, 32AD, Tea Development Benefit under section 33AB, Site Restoration benefit under section 33ABA, Scientific Research benefit under section 35, accelerated capital deduction for specified business under section 35AD, agricultural extension project benefit under section 35CCC, skill development project under section 35CCD and the benefit available under provisions of Chapter VI-A under the heading "C-Deductions in respect of certain incomes" i.e. 80IA, 80IB, 80IC, etc.. However, deduction under section 80JJAA in respect of additional employment will be available to such companies.

Further, such companies shall not be eligible to set off any loss carried forward from any earlier assessment year if such loss is attributable to any of the above deductions/incentives. Accordingly, if there is any carried forward loss, the same has to be adjusted by ignoring the deduction/incentives, if any, claimed under any of the above clauses.

Moreover, depreciation in such cases shall be computed in the manner as will be prescribed. It may be relevant to point out that apparent intention is to allow reduced rate of depreciation. It may be noted that similar provision of prescribing reduced depreciation was there in the section 115BA inserted by the Finance Act, 2016 when concession tax rate of 25 per cent was provided for Companies incorporated on or after 1st day of March, 2016 and engaged in the business of manufacture or production of any article or thing. In this regard, it may be noted that a proviso has been inserted under sub-rule (1) of Rule 5 vide Notification No. 103/2016 dated 7th November, 2016 with effect from 1st April 2016 to provide that that in case of a domestic company which has exercised option to pay concessional tax under 115BA, the allowance in respect of depreciation of any block of assets entitled to more than forty per cent shall be restricted to forty per cent on the written down value of such block of assets. However, it may be relevant to point out that the post the amendment of Appendix 1 vide Notification No. 103/2016 dated 7th November, 2016 with effect from 1st April, 2017, depreciation allowance in respect of all the assets has been capped at 40 per cent. Thus, the normal rate of depreciation prescribed in Appendix-1 continues to be applicable in respect of such domestic companies who have opted to pay tax at concessional rate under section 115BA. Considering this, there may not be any further reduction in the rate of depreciation applicable to such companies which opt for this reduced rate of tax under this new section 115BAA.

5. NO LIABILITY TO PAY MINIMUM ALTERNATE TAX (MAT) IF COMPANY OPTS TO PAY TAX AT ABOVE CONCESSIONAL RATE UNDER SECTION 115BAA

The above companies having opted for concessional rate of 22 per cent (effective rate 25.17 per cent) under newly inserted section 115BAA will have an additional benefit as there will be no liability to pay minimum alternate tax (MAT) under section 115JB. The Ordinance has amended section 115JB by inserting a new sub clause (ii) in sub section (5A) to provide that section 115JB shall not be applicable to a company which has exercised the option to be taxed at concessional rate under this new section 115BAA.

The above benefit of exemption from paying MAT in substance may not be much beneficial as with the prohibition of exemption/deductions in respect of income of SEZ allowable under section 10AA, Chapter-VIA heading C and other incentives, the difference in the book profit and the income computed under normal provision may not be much. The difference now in such cases will be mainly in the method/rate of depreciation charged under the Companies Act and the rate prescribed under the Income Tax Rules, disallowances or deductions under section 43B, 40(a)(i), 40(a)(ia), etc. Thus, such companies will not normally otherwise be liable for MAT.

However, non-applicability of MAT will certainly have some other benefits as discussed hereunder:

a. No liability under MAT if there is no capital gain after indexation

Presently, a company is required to pay MAT on the amount received by it in respect of sale of capital asset if such amount is more than the cost of acquisition despite the fact that there is no capital gain after taking into account indexed cost of acquisition. With the abolition of MAT in respect of those companies which have opted for this new provision, there will be no liability to pay MAT in respect of such difference. Further, long term capital gains are chargeable to tax at 20 per cent with the benefit of indexation available in respect of cost of acquisition and cost of improvement. Such tax amount, if computed as a percentage of the gain amount without applying indexation, it may fetch a number below 15 per cent. In such cases as well, the companies will benefit from non-applicability of MAT.

b. No liability under MAT in respect of income chargeable to tax at rate lower than rate of MAT

A company which is liable to pay tax in respect of any income which is chargeable to tax at special rates under Chapter XII, which are less than the rate of MAT, then such companies will benefit from such amendment. For instance, long term capital gain on sale of equity shares, unit of an equity oriented fund and unit of a business trust are liable to tax at the rate of 10 per cent under section 112A. Such gains are otherwise chargeable under MAT at 18.5 per cent (15 per cent now). In such cases, the companies will benefit from non-applicability of MAT.

c. Credit of carried forward MAT credit

Another issue will be of carried forward MAT credit. As per the existing provision of section 115JAA, credit is allowed of tax paid under MAT i.e. section 115JB of the difference between the tax payable by the assessee on his total income in the subsequent year and the MAT liability of that subsequent year. With the non-applicability of MAT provision, there will be no MAT liability in subsequent year and hence such company who opt for this new provision shall be in a position to claim credit of carried forward MAT against its entire current tax liability. Thus, it can be a big bonanza of zero tax for such companies which are having substantial amount of carried forward MAT. It is to be noted that amendment only has been made in section 115JB to provide that this section will not be applicable and there is no amendment in section 115JAA under which credit of carried forward MAT is allowed against regular tax liability.

d. Aggregate of carried forward loss and unabsorbed depreciation will be available for deduction against income computed under the normal provisions

Another benefit with the non-applicability of MAT will be on account of carried forward loss. Under MAT provisions, lower of unabsorbed depreciation or business loss is allowed to be set off while computing book profit liable for MAT whereas in the normal computation, aggregate of carried forward loss and unabsorbed depreciation is allowed to be set off.

e. Principal and/or interest waiver to Non-performing assets (NPAs) will not attract MAT

In case of NPAs, if a debt restructuring measure is implemented, the outcome of compromise or such measure is likely to result in a situation where substantial part of debt owed by the borrower company may be waived by the lenders. The borrowing companies may consequently write back such liabilities in their books by credit to Profit & Loss statement as required by applicable Accounting Principles. Once such liabilities are written back in the books of account by credit to the profit and loss account, the same becomes part of the book profit and hence attracts MAT despite having huge carried forward unabsorbed depreciation and business losses which are allowed to be adjusted under MAT only to the extent of lower of the two and that too as per the books of accounts. This has been causing great hardship to such companies as such companies were required to pay MAT despite being in heavy losses in the year of settlement with the bank/financial institution on the amount waived. Consequent to the abolition of MAT in respect of companies who opt to pay tax under this newly inserted section 115BAA, MAT provisions will not be applicable and consequently, the income will be computed under normal provisions where full benefit of aggregate of carried forward unabsorbed depreciation and business losses computed as per income tax provisions will be eligible for set off against the income computed under the normal provisions.

6. CAPITAL GAIN TAXABLE UNDER SECTION 111A, 112 AND 112A TO CONTINUE TO BE TAXED AT RATES PRESCRIBED UNDER SUCH SECTIONS

It is relevant to point out that sub-section (1) of this section 115BAA states that 'Notwithstanding anything contained in this Act but subject to provisions of this chapter....income tax payable in respect of the total income of a person..... shall at the option of such person be computed at the rate of 22 per cent'. It is to be noted here that tax rate of 22 per cent as per above section 115BAA is subject to the provisions of this chapter i.e. Chapter XII. Concessional rate on Capital gain in respect of STT paid short term capital gain is prescribed at the rate of 15 per cent under section 111A, long term capital gain tax rate of 20 per cent after benefit of indexation prescribed under section 112 and tax on STT paid long term capital gain in respect of sale of equity/ units of mutual funds post 1st April 2018 chargeable at the rate of 10 per cent without indexation under section 112A fall under this chapter. Thus, income by way of such capital gain will be chargeable at the above appropriate rate prescribed under these sections and not at the rate of 22 per cent. However, tax on other short term capital gain which is chargeable under the normal provisions does not fall under this chapter and the strict interpretation of total income will mean that such short term capital gain will also be chargeable at the concessional rate of 22 per cent under this new section 115BAA.

7. OPTION TO PAY TAX AT CONCESSIONAL RATE NEED TO BE EXERCISED BEFORE FURNISHING RETURNS OF INCOME AND CANNOT BE SUBSEQUENTLY WITHDRAWN

For claiming concessional rate of 22 per cent, such company shall be required to exercise the option before the due date of furnishing the return under section 139(1) of the Act. However, there is no restriction that such option is to be exercised in the current year itself. Thus, such option may be exercised in the subsequent years as well. However, it has been provided once this option has been exercised for any year it cannot be subsequently withdrawn for the same or any other assessment year. Thus, option once exercised under this section will be applicable in perpetuity to the company in subsequent assessment years.

8. EVALUATION OF TAX LIABILITY UNDER EXISTING RATES AND NEWLY INSERTED SECTION 115BAA

The above amendment will ideally suit by and large to all companies particularly those providing services, engaged in trading except a few companies which are eligible to claim deduction under section 10AA in respect of special economic zone, or which are eligible to claim deduction under section 80IA, 80IB etc. or companies which have acquired or installed new plant and machinery and accordingly the claim of initial depreciation of 20 per cent in respect of such new plant & machinery acquired is substantial. However, as pointed out earlier, even such companies who are claiming the said deductions and exemptions have the option to pay tax under this newly inserted section 115BAA from subsequent year when it has exhausted the benefit of deduction/incentive under above provisions. Accordingly, it will be advisable to work out the tax liability under the existing provision i.e. at the rate of 25 per cent in case turnover during financial year does not exceed Rs. 400 crores and 30 per cent in case where turnover exceeds Rs. 400 crores (plus surcharge and health and education cess as applicable) and after claiming various deductions/incentives and the option given under this newly inserted section 115BAA i.e. at the rate of 22 percent (plus surcharge and health and education cess as applicable). In case it is found that the tax liability under this new provision consequent to denial of various deductions/exemptions is more than the tax liability under the normal provision, then the company may not opt for this reduced rate and may opt for this new provision in subsequent year when tax liability under this new provision is less than the normal provision. However, it should be noted that once an option is exercised under this new provision it will be applicable for subsequent years as well. Thus, this exercise need to be carried out keeping in mind the future deduction/incentive, if any, to which such company may be eligible to claim.

9. REDUCED RATE TO APPLY FROM ASSESSMENT YEAR 2020-21 I.E. INCOME EARNED DURING THE CURRENT FINANCIAL YEAR STARTING FROM 1ST APRIL 2019

This amendment will be applicable for assessment year 2020-21 i.e. the income of the current financial year 2019-20.

B. CONCESSIONAL RATE OF TAX OF 15 PER CENT FOR NEW COMPANIES ENGAGED IN MANUFACTURING AND PRODUCTION

1. TAX RATE OF 15 PER CENT (EFFECTIVE TAX RATE OF 17.16 PER CENT) FOR NEW MANUFACTURING COMPANIES

The Taxation Laws (Amendment) Ordinance, 2019 has inserted another section 115BAB, to boost manufacturing in India, providing an option of concessional rate of tax of 15% to new domestic companies setup and registered on or after 1st October, 2019 and engaged solely 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. This benefit will available to all such domestic companies which commence manufacturing on or before 31st day of March, 2023. Thus, the concessional rate is not for short term but applicable for all such companies which are set up and registered and commence manufacturing during the period spread over from 1st October 2019 to 31st March 2023 i.e. three and a half years. The surcharge applicable on such tax shall be 10 percent irrespective of the income of the company with health and education cess at the rate of 4 per cent. Thus, the effective tax rate will be 17.16 per cent.

2. ELIGIBILITY CRITERIA TO OPT FOR CONCESSIONAL RATE OF TAX UNDER SECTION 115BAB

It is to be noted that this provision is applicable to domestic companies which means Indian company i.e. all companies formed and registered in India including by Multinational Companies but does not include branch or permanent establishment of foreign companies. It is to be noted that this benefit is available only to such companies which have been set up and registered on or after 1st October, 2019 and accordingly the existing companies cannot be used for setting up a new business. A new company needs to be incorporated so that its date of registration is also on or after 1st October, 2019 and such company needs to commence manufacturing on or before 31st March, 2023. Further, such company cannot be formed by splitting up or reconstruction of a business already in existence. Also, such companies cannot use any machinery or plant previously used for any purpose. However, a company may use previously used plant and machinery as long as its value does not exceed 20 per cent of the total value of the plant and machinery of the company. Tax rates in respect of other entities such as partnership firm, LLP, Individuals, HUF, etc. shall continue to be as notified in the Finance (No. 2) Act, 2019.

3. CONCESSIONAL RATE UNDER THIS NEW SECTION 115BAB IS ASSESSEE BASED NOT MANUFACTURING UNIT BASED - EXISTING COMPANY NEED TO INCORPORATE A NEW COMPANY FOR AVAILING CONCESSIONAL RATE OF 15 PER CENT

This new section 115BAB provides for concessional rate of 15 per cent (effective rate 17.16 per cent) on total income of a domestic company set up and registered on or after 1st October 2019 and which is not engaged in any business other than the business of manufacturing or production. Hence, this deduction will not be available to an existing company even if it sets up a new unit of manufacturing or production. Thus, the existing company in case it intends to avail benefit of this concessional rate, need to set up a separate company may be a subsidiary company. It would have been ideal if this benefit would have been extended in respect of income derived from a new industrial undertaking /unit set up on or after 1st October 2019 from the business of manufacturing or production of any article or thing.

4. DEDUCTIONS/INCENTIVES TO BE FORGONE IN CASE COMPANY OPTS TO PAY TAX AT CONCESSIONAL RATE UNDER SECTION 115BAB

The conditions imposed in order for a company to be eligible to opt for concessional rate of tax under section 115BAB are somewhat similar to the conditions imposed under new section 115BAA. Such companies, who opts to pay tax at concessional rate under section 115BAB, while computing the total income have to forego deduction on account of SEZ under section 10AA, additional initial depreciation allowable at the rate of 20 per cent under section 32(1)(iia), investment allowance in respect of new plant and machinery under section 32AC, 32AD, Tea Development Benefit under section 33AB, Site Restoration benefit under section 33ABA, Scientific Research benefit under section 35, accelerated capital deduction for specified business under section 35AD, agricultural extension project benefit under section 35CCC, skill development project under section 35CCD and the benefit available under provisions of Chapter VI-A under the heading "C-Deductions in respect of certain incomes" i.e. 80IA, 80IB, 80IC, etc.. However, deduction under section 80JJAA in respect of additional employment will be available to such companies.

Further, such company shall not be eligible to set off any loss carried forward from any earlier assessment year if such loss is attributable to any of the above deductions. Accordingly, if there is any carried forward loss the same has to be adjusted by ignoring the deduction if any claimed under any of the above clauses. It may be noted that though this section provides for restricting carried forward loss without deduction and incentive, however, considering the fact that such companies are new and are required to exercise the option under this section in the very first year of the return of income, practically there will be no such carried forward loss which will be attributable to any of the restricted deduction/incentive.

Another condition prescribed, similar to that prescribed under section 115BAA, is that the depreciation in such cases shall be computed in the manner as will be prescribed. It may be relevant to point out here as well that apparent intention is to allow reduced rate of depreciation. As mentioned earlier, it may be reiterated that a similar provision of prescribing reduced depreciation was there in the section 115BA inserted by the Finance Act, 2016 when concession tax rate of 25 per cent was provided for Companies incorporated on or after 1st day of March, 2016 and engaged in the business of manufacture or production of any article or thing. In this regard, it may be noted that a proviso has been inserted under sub-rule (1) of Rule 5 vide Notification No. 103/2016 dated 7th November, 2016 with effect from 1st April 2016 to provide that that in case of a domestic company which has exercised option to pay concessional tax under 115BA, the allowance in respect of depreciation of any block of assets entitled to more than forty per cent shall be restricted to forty per cent on the written down value of such block of assets. However, it may be relevant to point out that the post the amendment of Appendix 1 vide Notification No. 103/2016 dated 7th November, 2016 with effect from 1st April, 2017, depreciation allowance in respect of all the assets has been capped at 40 per cent. Thus, the normal rate of depreciation prescribed in Appendix-1 continues to be applicable in respect of such domestic companies who have opted to pay tax at concessional rate under section 115BA. Considering this, there may not be any further reduction in the rate of depreciation applicable to such companies which opt for this reduced rate of tax under this new section 115BAB.

5. NO LIABILITY TO PAY MINIMUM ALTERNATE TAX (MAT) IF COMPANY OPTS TO PAY TAX AT ABOVE CONCESSIONAL RATE UNDER SECTION 115BAB

The above companies who opts for concessional rate of 15 per cent (effective rate 17.16 per cent) under newly inserted section 115BAB will have an additional benefit as there will be no liability to pay minimum alternate tax (MAT) under section 115JB. The Ordinance has amended section 115JB by inserting a new sub clause (ii) in sub section (5A) to provide that section 115JB shall not be applicable to a company which has exercised the option to be taxed at concessional rate under this new section 115BAB.

The above benefit of exemption from paying MAT in substance may not be much beneficial as with the prohibition of exemption/deductions in respect of income of SEZ allowable under section 10AA, Chapter-VIA heading C and other incentives, the difference in the book profit and the income computed under normal provision may not be much. The difference now in such cases will be mainly in the method/rate of depreciation charged under the Companies Act and the rate prescribed under the Income Tax Rules, disallowances or deductions under section 43B, 40(a)(i), 40(a)(ia), etc. Thus, such companies will not normally otherwise be liable for MAT.

However, non-applicability of MAT will certainly have some other benefits as discussed hereunder:

a. No liability under MAT if there is no capital gain after indexation

Presently, a company is required to pay MAT on the amount received by it in respect of sale of capital asset if such amount is more than the cost of acquisition despite the fact that there is no capital gain after taking into account indexed cost of acquisition. With the abolition of MAT in respect of those companies which have opted for this new provision, there will be no liability to pay MAT in respect of such difference. Long term capital gains are chargeable to tax at 20 per cent with the benefit of indexation available in respect of cost of acquisition and cost of improvement. Such tax amount, if computed as a percentage of the gain amount without applying indexation, it may fetch a number below 15 per cent. In such cases as well, the companies will benefit from non-applicability of MAT.

b. No liability under MAT in respect of income chargeable to tax at rate lower than rate of MAT

A company which is liable to pay tax in respect of any income which is chargeable to tax at special rates under Chapter XII, which are less than the rate of MAT, then such companies will benefit from such amendment. For instance, long term capital gain on sale of equity shares, unit of an equity oriented fund and unit of a business trust are liable to tax at the rate of 10 per cent under section 112A. Such gains are otherwise chargeable under MAT at 18.5 per cent (15 per cent now). In such cases, the companies will benefit from non-applicability of MAT.

c. Aggregate of carried forward loss and unabsorbed depreciation available under normal provisions

Another benefit with the non-applicability of MAT will be on account of carried forward loss. Under MAT provisions, lower of unabsorbed depreciation or business loss is allowed to be set off while computing book profit liable for MAT whereas in the normal computation, aggregate of carried forward loss and unabsorbed depreciation is allowed to be set off.

6. CAPITAL GAIN TAXABLE UNDER SECTION 111A, 112 AND 112A CONTINUE TO BE TAXED AT RATES PRESCRIBED UNDER SUCH SECTIONS

It is relevant to point out that sub-section (1) of this section 115BAB states that 'Notwithstanding anything contained in this Act but subject to provisions of this chapter....income tax payable in respect of the total income of a person..... shall at the option of such person be computed at the rate of 15 per cent'. It is to be noted here that tax rate of 15 per cent as per above section 115BAA is subject to the provisions of this chapter i.e. Chapter XII. Concessional rate on Capital gain in respect of STT paid short term capital gain is prescribed at the rate of 15 per cent under section 111A, long term capital gain tax rate of 20 per cent after benefit of indexation prescribed under section 112 and tax on STT paid long term capital gain in respect of sale of equity/ units of mutual funds post 1st April 2018 chargeable at the rate of 10 per cent without indexation under section 112A fall under this chapter. Thus, income by way of such capital gain will be chargeable at the above appropriate rate prescribed under these sections and not at the rate of 15 per cent. However, tax on other short term capital gain which is chargeable under the normal provisions does not fall under this chapter and the strict interpretation of total income will mean that such short term capital gain will also be chargeable at the concessional rate of 15 per cent under this new section 115BAB.

7. OPTION TO PAY TAX AT CONCESSIONAL RATE TO BE EXERCISED BEFORE FURNISHING THE FIRST RETURNS OF INCOME AND CANNOT BE SUBSEQUENTLY WITHDRAWN

For claiming concessional rate of 15 per cent, such company shall be required to exercise the option before the due date of furnishing the very first of the returns under section 139(1) of the Act. Thus, as against the provision of section 115BAA where an option has been given to avail benefit from the year when such company intends to opt for such benefit, under this clause there is no such option. Either such company has to exercise the option in the very first year or forgo for all times. The implication of this will be that a company has to make a choice in the very first year. In case a company does not opt for this provision, then it shall not be eligible for all times to come. However, once this option has been exercised by a company it cannot be subsequently withdrawn for the same or any other assessment year. Thus, option once exercised under this section will be applicable in perpetuity to the company.

8. CHALLENGES IN OPTING CONCESSIONAL RATE OF 15 PER CENT UNDER SECTION 115BAB

There is no condition/limitation on account of turnover under section 115BAB but the company should not be engaged in any business other than 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. This clause apparently is very restrictive. There may be a question raised in case such company does some trading of the items it is engaged in manufacturing or production to meet the business requirement or provide some services. There may be a question raised that the company has failed to meet the condition prescribed which is worded negatively i.e. 'not engaged in any business other than the business of manufacturing or production'. Further, there may also a question raised as to whether a company that is engaged in the business of generation of power can be said to be eligible to opt for the concessional rate of 17.16 per cent under section 115BAB as there have been disputes in the past on the issue as to whether the generation of power means production of an article or thing.

Further, there may be a question on the income such companies may have from interest in respect of surplus money or accumulated profits. It may have some rental income in respect of assets owned by it or capital gain arising from the sale of assets or investments held by it. There is no clarity whether in such case company will lose benefit of concessional rate of 15 per cent or only such income which is not from the business of manufacturing or production will be taxed at a rate other than the 15 per cent. As noted earlier, sub-section (1) of this section 115BAB states that 'Notwithstanding anything contained in this Act but subject to provisions of this chapter.... income tax payable in respect of the total income of a person shall at the option of such person be computed at the rate of 15 per cent'. Meaning of this will be that the total income of such company will be taxed at the rate of 15 per cent. The total income of such company obviously will include income by way of interest, rent, etc. if any. Apparently, earning such income by way of interest or rent etc. do not violate the above condition since earning interest income and rental income does not mean carrying on or engagement in any other business. Income from interest/dividend from investments is normally chargeable as income from other sources and income from rent in respect of land and building is normally chargeable as income from house property. Thus, earning such income is not likely to be seen as a violation of such condition.

9. CONSEQUENCES OF INDULGING IN ANY OTHER BUSINESS OTHER THAN MANUFACTURING OR PRODUCTION

As pointed out earlier, this benefit of concessional tax is available only to such companies which are not engaged in any business other than the business of manufacturing or production. Thus, such companies need to ensure that it does not carry on any other business even trading or providing services for all times to come. In case such company inadvertently in some subsequent year does some activity or carry on business which is beyond the business permissible, then it may not be eligible to claim the concession rate of tax of 15 per cent. At the same time, this may give an option to the company to exit this provision by committing default which exit as explained above is otherwise prohibited.

In case a company engages in any business other than the business of manufacturing or production in any subsequent year, then it may opt to pay tax for such year at the concessional rate of tax of 22 per cent (effective tax rate of 25.16 per cent) under section 115BAA. Such option will have to be exercised on or before the due date of furnishing of return of income under section 139(1) of such year. It is relevant to point out that there is no condition prescribed under section 115BAA that the option to pay tax is to be exercised in the first year itself. Thus, such option may be exercised in the subsequent years as well. However, once this option has been exercised for any year, it cannot be subsequently withdrawn for the same or any other assessment year.

It is relevant to point out that in case a company pays tax at the concessional rate of 17.16 per cent under section 115BAB for any year and subsequently, during the assessment proceedings, it is disputed by the assessing officer that the company is engaged in any business other than the business of manufacturing or production, then such company will not have the option to pay tax at the concessional rate of 25.16 per cent under section 115BAA. This is because the option to pay tax at concessional rate under section 115BAA is to be exercised on or before the due date of furnishing the return of income under section 139(1) of the Act which will obviously not be the case. Such company will accordingly be liable to pay tax for such year at the rates specified in the First Schedule to the Finance (No. 2) Act, 2019 i.e. 25 per cent (plus surcharge and cess as applicable) in case its turnover in previous year 2017-18 does not exceed Rs. 400 crores or 30 per cent (plus surcharge and cess as applicable) in case its turnover exceeds Rs. 400 crores.

10. APPLICABILITY OF TRANSFER PRICING PROVISIONS

It is to be noted that provision of section 92BA are being amended so as to apply transfer pricing provision on the business of these new companies. In this regard, a new clause (va) has been inserted in section 92BA to apply specified domestic transfer pricing provision in respect of any business transacted between such company and its associate enterprises.

11. REDUCED RATE TO APPLY FROM ASSESSMENT YEAR 2020-21 I.E. INCOME EARNED DURING THE CURRENT FINANCIAL YEAR STARTING FROM 1st OCTOBER, 2019

This amendment will be applicable for assessment year 2020-21 i.e. the income of the current financial year 2019-20.

C. MINIMUM ALTERNATE TAX (MAT) RATE REDUCED FROM 18.5 PER CENT TO 15 PER CENT

The Taxation Laws (Amendment) Ordinance, 2019 has inserted two new sections 115BAA and 115BAB to provide an option for domestic companies to pay tax at concessional rate of 25.17 per cent and 17.16 per cent respectively inclusive of surcharge and health and education cess if such companies do not claim any specified deduction/exemption as discussed above. Further, such companies are also not required to pay MAT. However, some companies who have been claiming the specified deductions/exemptions may find it more economical to continue with the existing rates and accordingly may opt to switch over to such reduced rates in the subsequent years once the tax holiday/exemption period is over. In order to provide relief to such companies who continue to pay tax as per the First Schedule to the Finance (No.2) Act, 2019 the Taxation Laws (Amendment) Ordinance, 2019 has reduced the MAT rate from 18.5 per cent to 15 per cent. The net savings in taxes that arises, to different category of domestic companies based on the amount of book profit, who continue to pay taxes as per the First Schedule to the Finance (No. 2) Act, 2019 can be seen from the below table:

Book profits	MAT liability prior to amendment		MAT liability subsequent to amendment		Savings in taxes
	MAT Rate: 18.5%		MAT Rate: 15%		
	Surcharge	Effective tax rate*	Surcharge	Effective tax rate*	
Upto Rs. 1 crore	0%	19.24%	0%	15.60%	3.64%
More than Rs. 1 crore but upto Rs. 10 crores	7%	20.59%	7%	16.69%	3.89%
More than Rs. 10 crores	12%	21.55%	12%	17.47%	4.08%

* Effective tax rates are inclusive of surcharge, wherever applicable and health and education cess @ 4%

As per the above table, a company will enjoy saving in taxes to the tune of 3.64 per cent in case its book profits does not exceed Rs. 1 crores, 3.89 per cent in case its book profits exceeds Rs. 1 crores but does not exceed Rs. 10 crores and 4.08 per cent in case its book profits exceeds Rs. 10 crores.

This amendment will be applicable for assessment year 2020-21 i.e. the income of the current financial year 2019-20.

D. OTHER AMENDMENTS

1. ENHANCED SURCHARGE TO NOT APPLY ON CAPITAL GAIN ON SALE OF EQUITY SHARE OR EQUITY ORIENTED MUTUAL FUND.

The Taxation Laws (Amendment) Ordinance, 2019 has amended section 2 of the Finance (No.2) Act, 2019 to provide that enhance surcharge on individual HUF, AOP, BOI including FPI of 25 per

cent in case income exceeds Rs.2 Crore and at the rate of 37 per cent in case income exceeds Rs.5 Crore shall not be applicable in respect of capital gain arising on sale of equity share in a company or a unit of equity oriented fund or unit of a business trust liable for security transaction tax. This surcharge shall also not apply on capital gain arising on sale of any security including derivatives in the hands of foreign portfolio investor.

2. NO TAX ON BUY BACK OF SHARE OF LISTED COMPANIES BEFORE 5TH JULY, 2019

The Taxation Laws (Amendment) Ordinance, 2019 has amended the provision of section 115QA which was amended by the Finance (No.2) Act, 2019 exempting tax on buy back of share of listed companies which have made a public announcement of such buy back before 5th July, 2019. It may be relevant to point out that the Finance (No.2) Act, 2019 has extended the levy of tax on buy back of share on listed companies with effect from 5th July, 2019 with the result that many listed companies which have initiated the process of buy back had to pay further tax on such buy back.

E. INADVERTENT ERRORS

1. EXIT ROUTE TO COMPANIES WHO HAVE OPTED FOR CONCESSIONAL RATE OF TAX UNDER SECTION 115BA

The Finance Act, 2016 has inserted this section 115BA allowing concession rate of 25 per cent in respect of companies incorporated on or after 1st March, 2016 and carry on 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. In this section there was a provision as in the new provision 115BAB to the effect that option once exercised cannot be subsequently withdrawn for the same or any other assessment year. Thus, as on date, those companies which have exercised the option of concession rate of tax at the rate of 25 per cent under this section 115BA are not eligible to switch over to any new provision including the newly inserted section 115BAA where tax rate has been reduced for all companies to 22 per cent. The Taxation Laws (Amendment) Ordinance, 2019 in order to provide an exit route has inserted a proviso that where such company exercises option under section 115BAB, the option under the old provision i.e. 115BA may be withdrawn. However, there appears to be an apparent error as option under section 115BAB can be exercised by only those companies which have been incorporated on or after 1st October, 2019 and hence all such companies which have already opted for provision of section 115BA cannot switch over to section 115BAB. It appears that the amendment was intended to allow switch over to section 115BAA where concession rate of 22 per cent is applicable and inadvertently section 115BAB has been mentioned in the ordinance. This amendment will be applicable for assessment year 2020-21 i.e. the income of the current financial year 2019-20.

2. DOMESTIC COMPANIES NO TO USE ANY BUILDING PREVIOUSLY USED AS A HOTEL OR A CONVENTION CENTRE TO BE ELIGIBLE TO OPT FOR 15% UNDER SECTION 115BAB

The Taxation Laws (Amendment) Ordinance, 2019 has inserted a new section 115BAB providing an option of concessional rate of tax of 15% to new domestic companies setup and registered on or after 1st October, 2019 and engaged solely in the business of manufacturing or production if such company commences manufacturing or production on or before 31st day of March, 2023.

One of the conditions prescribed under this newly inserted section 115BAB is that the domestic company should not use any building previously used as a hotel or a convention centre in order to be eligible to opt for such concessional rate. However, there appears to be an apparent copy paste error here since such condition is rather unusual and abnormal in respect of the manufacturing industry.

It may be relevant to point out here that the provisions of this newly inserted section 115BAB is similar to the provisions of section 115BA introduced earlier vide Finance Act 2016 to provide for concessional rate of tax of 25% in respect of domestic companies setup and registered on or after 1st March, 2016 and engaged solely in the business of manufacturing or production of any article or thing. The only main difference between such provisions is that section 115BAB provides for an option of concessional rate to those domestic companies that are set up and registered on or after 1st October 2019 whereas the earlier section 115BA provided such companies that are set up and registered on or after 1st March 2016.

It is relevant to point out here that the earlier provision did not provide for any such restriction that a domestic company should not use any building previously used as a hotel or a convention centre in order to be eligible to opt for the concessional rate of tax. Further, it is may also be noted that no such similar restriction has been placed earlier while extending the benefit of any tax incentive on manufacturing of production of any article of thing under Chapter VI. Thus, it appears that such condition is as a result of copy paste error which will be rectified.

SUMMARY OF TAX RATES IN FORCE CONSEQUENT TO AMENDMENT MADE BY THE ORDINANCE

Income	Option to pay tax at concessional rates under the provisions of the Income Tax Act, 1961			Tax rates under First Schedule to the Finance (No. 2) Act, 2019		
	Domestic Manufacturing Companies incorporated on or after 1st October 2019 (Section 115BAB)	Domestic Companies (Section 115BAA)	Certain domestic manufacturing companies incorporated on or after 1st March 2016 (Section 115BA)	Domestic Companies whose turnover in Previous Year 2017-18 does not exceed Rs. 400 crores	Domestic Companies whose turnover in Previous Year 2017-18 exceeds Rs. 400 crores	
	Tax rate	Effective tax rate*	Sur-charge	Tax rate	Effective tax rate*	Sur-charge
Upto Rs. 1 crore	15%	17.16	10%	25%	26.00	0%
More than Rs. 1 crore but upto Rs. 10 crores	15%	17.16	10%	25%	27.82	7%
More than Rs. 10 crores	15%	17.16	10%	25%	29.12	12%
	Effective tax rate*	Sur-charge	Tax rate	Effective tax rate*	Sur-charge	Effective tax rate*
Upto Rs. 1 crore	31.20	0%	30%	31.20	0%	31.20
More than Rs. 1 crore but upto Rs. 10 crores	33.38	7%	30%	33.38	7%	33.38
More than Rs. 10 crores	34.94	12%	30%	34.94	12%	34.94
INCOME TAX RATES IN RESPECT OF INCOME CHARGEABLE UNDER THE NORMAL PROVISIONS OF THE ACT						
MINIMUM ALTERNATE TAX RATES						
Book profits under section 115JB	Tax rate	Effective tax rate*	Sur-charge	Tax rate	Effective tax rate*	Sur-charge
Upto Rs. 1 crore				15%	15.60	0%
More than Rs. 1 crore but upto Rs. 10 crores	MAT not applicable	MAT not applicable		15%	16.69	7%
More than Rs. 10 crores				15%	17.47	12%

* Effective tax rates are inclusive of surcharge, wherever applicable and health and education cess @ 4%



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