UPDATES

Interim Budget 2024 – Key Highlights

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This update covers:

The Indian Finance Minister presented the Interim Budget (**Interim Budget 2024**) on 1 February 2024 setting the tone for sustainable development and inclusive growth as part of the government's vision for a '*viksit*' (developed) India by 2047. To this end, the government's policy focus is on encouraging foreign investment by negotiating bilateral investment treaties centred on '*first develop India*'. The other drivers of policy decisions are empowering the youth and encouraging the private sector to ramp up research and innovation by providing long-term financing/re-financing at low or nil interest rates and introducing tax reforms.

The Interim Budget, announced on 1 February 2024, focuses on policy proposals around sustainable development, infrastructure, agriculture, and tax reforms. This update analyses the key highlights of the Interim Budget 2024.

To further India's commitment to achieve '*net zero*' by 2070, the policy announcements also contain measures such as providing free electricity through rooftop solarisation, harnessing the potential of wind energy, capacity building for coal gasification and liquification, and mandating blended compressed biogas and compressed natural gas for transportation through pipes, and piped natural gas for domestic use, among others.

Ahead of the comprehensive budget to be announced after the general elections take place, the key highlights of the Finance Minister's speech on the Interim Budget 2024 are:

1 Sustainable development

a. ***Rooftop solarisation***: The government plans to provide free monthly electricity to one crore households through rooftop solarisation. This initiative aims to bring about various benefits, such as annual savings of up to INR 18,000 for households, opportunities for entrepreneurship in supply and installation of solar panels and employment prospects for youth. We expect that India will now have a very high potential for the solar panels manufacturing and trading industry.

b. ***Green energy***: To achieve the '*net-zero*' commitment by 2070, measures such as viability gap funding for offshore wind energy, mandating phased blending of compressed biogas in CNG and PNG, building of coal gasification capacities, offering financial aid for biomass aggregation machinery, new schemes for bio-manufacturing, new schemes for promoting climate-resilient activities for Blue Economy 2.0 are being announced. The industries in the above sectors have a huge opportunity for rapid growth in the next several decades.

These measures will reduce our dependency on imported natural gas and allied products and hence reduce India's huge import bill. These policies seem to be the right steps to reach the net zero target by 2070. We can expect certain tax incentives for these businesses in the comprehensive budget to be presented later this year.

2 Infrastructure

The capital expenditure outlay for next year is increased by 11.1% over last year's capital expenditure on infrastructure, reaching 3.4% of the gross domestic product (GDP). Three major economic railway corridor programs will be implemented: energy, mineral, and cement corridors; port connectivity corridors; and high traffic density corridors. Additionally, projects for port connectivity, tourism infrastructure, and amenities will be initiated on islands like Lakshadweep to boost domestic tourism.

India has already moved fast in the infrastructure development space with state-of-the-art expressways, ports, airports, sea-links, tunnels, metro rails, *vande-bharat* trains and many more landmark projects. Infrastructure is the backbone of our economy and the allocations towards the infrastructure sector should mean that the economy will grow in leaps and bounds.

3 Agriculture

Efforts to boost value addition in agriculture and raise farmers' income are being strengthened. The government will promote both private and public investments in post-harvest activities, such as aggregation, modern storage, efficient supply chains, primary and secondary processing, along with marketing and branding. This will ensure a faster growth trajectory for the agricultural sector.

4 Direct tax

a. ***Withdrawal of small outstanding direct tax demands***: The Finance Minister, in her budget speech, has proposed the withdrawal of petty, non-verified, non-reconciled or disputed direct tax demands up to INR 25,000 pertaining to the period up to financial year 2009-10 and up to INR 10,000 for financial years 2010-11 to 2014-15.

   This move is expected to benefit around ten million taxpayers.

b. ***Exemption to investment division of an offshore banking unit***: Section 10(4D) of the Income-tax Act, 1961 (**ITA**) provides an exemption for specified income of investment division of an offshore banking unit. An "*investment division of an offshore banking unit*" is defined as the investment division of a banking unit of a non-resident located in an International Financial Services Centre (**IFSC**) and which has commenced its operations on or before 31 March 2024.

   It is proposed to extend the date for commencing operations from 31 March 2024 to 31 March 2025. Consequently, the specified income of the investment division of an offshore banking unit will remain exempt if it initiates operations on or before 31 March 2025. This extension should encourage offshore banks to set up units in IFSC.

c. ***Exemption to royalty or interest income received by a non-resident from the lease of aircraft or a ship***: Section 10(4F) of ITA provides an exemption for the income of a non-resident by way of royalty or interest, arising from the lease of an aircraft or a ship, when paid by a unit of an IFSC, provided that the unit commenced its operations on or before 31 March 2024.

   It is proposed to extend the date of commencement of operations by IFSC unit from 31 March 2024 to 31 March 2025. This extension will encourage aircraft and ship leasing businesses to set up in IFSC.

d. ***Exemption to sovereign wealth fund or foreign pension fund***: Section 10(23FE) of ITA provides that income in the nature of dividends, interest, or long-term capital gains from infrastructure investment made by sovereign wealth fund, or a foreign pension fund will be exempt from tax, subject to the fulfilment of certain conditions. The exemption under this provision shall be available if the investment is made between 1 March 2020 and 31 March 2024 in the specified entities.

   It is proposed to extend the deadline for making investments from 31 March 2024 to 31 March 2025. This extension will promote funding of the infrastructure development goals of the country.

e. ***Deduction to IFSC unit on the transfer of an asset being an aircraft or a ship***: A Scheduled Bank, a foreign bank, or a unit of an IFSC is eligible to claim a deduction under Section 80LA of ITA for income arising from the transfer of an asset being an aircraft or a ship, which was leased by an IFSC unit. For a bank, 100% of the income is deductible for ten consecutive assessment years. In the case of an IFSC unit, 100% of the income is deductible for ten consecutive assessment years out of 15 years. However, the deduction for this income is only allowed if the unit commenced operations on or before 31 March 2024.

   It is proposed to extend the commencement of operations date from 31 March 2024 to 31 March 2025.

f. ***Tax holiday for eligible start-ups***: Section 80-IAC of ITA provides a tax holiday to start-ups (companies or LLPs) engaged in innovation, development or improvement of products or processes or services or a scalable business model with a high potential of employment generation or wealth creation. Such start-ups earning any profits and gains from their businesses are allowed a deduction of 100% of such profits and gains while computing their total taxable incomes. This deduction is allowed for three consecutive assessment years and can be claimed for any three such years out of the ten years starting from the year of incorporation of such start-ups.

   To claim this deduction, start-ups must fulfill some specific eligibility conditions, one of them being that they should be incorporated on or after 1 April 2016 but before 1 April 2024.

   It is proposed to extend this period of incorporation till 1 April 2025. This is yet another welcome measure, as part of the government's continuous efforts to boost start-up culture and encourage entrepreneurship. This should benefit a larger number of start-ups and help in beefing up the liquidity available with start-ups, aiding their development and expansion.

g. ***Tax collection at source for payments under the Liberalised Remittance Scheme***: Tax Collection at Source (**TCS**) rates applicable on payments under the Liberalised Remittance Scheme (**LRS**) were revised by way of a notification issued in June 2023. This has now been codified. The revised TCS rates are summarised below.

Payments	Rate of TCS
Purchase of overseas tour program package	5% till INR 7,00,000 and 20% thereafter
Medical treatment/education	5% if aggregate remittance exceeds INR 7,00,000
Education, where source of funds is through loan obtained from specified financial institution	0.5% if aggregate remittance exceeds INR 7,00,000
LRS for other purposes	20% if aggregate remittance exceeds INR 7,00,000

Individuals intending to remit payments for the aforementioned categories should take note of the prescribed TCS rates and limits. Notably, this could pose a cash flow issue for businesses as the TCS will be available as a credit when filing tax returns.

5 Indirect tax

a. ***Applicability of the Input Service Distributor mechanism***: The amendments proposed in the Finance Bill, 2024 aim to address a persistent concern, namely the mandatory applicability of the Input Service Distributor (**ISD**) mechanism. The issue of whether the Head Office (**HO**) of an entity is mandatorily required to get itself registered as an ISD for the purpose of distribution of Input Tax Credit (**ITC**) pertaining to common input services procured from third parties among various branch offices has been extensively debated from the onset of the Goods and Services Tax (**GST**) regime.

   Acknowledging the confusion among the taxpayers, the Central Board for Indirect Taxes and Customs (**CBIC**) had clarified, by way of a circular, that registration as ISD is not mandatory under the present provisions of the Central Goods and Services Tax Act, 2017 (**CGST Act**) on the recommendations of the GST Council.

   The GST Council had also suggested that appropriate amendments should be made in the CGST Act to make the ISD mechanism mandatory prospectively for the distribution of ITC of such common input services procured from third parties. Accordingly, amendments have now been proposed to be made in the CGST Act with the intent to make registration as ISD mandatory for a HO to distribute ITC of common input services. The taxpayers will now engage in renewed discussions regarding their existing arrangement for distribution of common ITC owing to the amendments proposed in the Finance Bill, 2024.

b. ***Penalty proposed for non-compliance with registration requirement of machines manufacturing specified products***: In July 2023, the CBIC outlined specific procedures for tobacco, pan masala, and similar product manufacturers regarding machine registration and monthly return filing. The Interim Budget 2024 introduces a stringent measure, levying a significant penalty of INR 1 lakh per unregistered machine used in the production of these items which fails to comply with the prescribed procedures. Furthermore, such non-compliant machinery faces a risk of seizure and confiscation, emphasising the government's tightened regulatory stance on these sectors.

c. ***Continuation of scheme for rebate of State and Central taxes and levies***: The Union Cabinet, on 1 February 2024, approved the continuation of the Scheme for Rebate of State and Central Taxes and Levies (**RoSCTL**) for export of apparel/garments made up to 31 March 2026. The RoSCTL was introduced to compensate the exporters for the State and Central Taxes and levies in addition to the Duty Drawback Scheme on export of apparel/garments by way of rebate.

The rebate of State taxes and levies comprise Value Added Tax (**VAT**) on fuel used in transportation, captive power, farm sector, mandi tax, duty of electricity, stamp duty on export documents, embedded State Goods and Services Tax (**SGST**) paid on inputs used in the manufacture and transportation of the goods. Whereas the rebate of Central taxes and levies comprises central excise duty on fuel used in transportation, embedded Central Goods and Services Tax (**CGST**) paid on inputs such as pesticides, fertilisers, etc., used in the production of raw cotton, and embedded CGST and Compensation Cess on coal used in the production of electricity.

The continuation of RoSCTL is welcomed by the textile sector as it will ensure stability and continuity in the policy regime.

Looking ahead

The government's development vision stays focused on infrastructure and foreign investment in India, with attention on agriculture, tourism, solar, electric, and green energy sectors. This is likely to lead to a rise in merger and acquisition activities and fresh investments in these areas. Existing major conglomerates in India are poised to expand their operations, and there may also be new entrants into these sectors from outside India. This interim budget has also placed a significant focus on IFSC, particularly in relation to offshore banking units and aircraft and ship leasing businesses.

As this is an interim budget, not many changes were expected on the tax front. Accordingly, the tax rates remained unchanged. One of the key expectations of the industry on extension of the deadline to avail the concessional tax rate of 15% for new domestic manufacturing companies, expiring on 31 March 2024, has not been extended. Consequently, new manufacturing companies now have only a brief two-month window to commence operations and qualify for the concessional tax rate of 15% as against the tax rate of 22%. On the indirect tax front, the Interim Budget 2024 refrains from addressing several crucial issues, such as the eagerly awaited Customs Amnesty Scheme, providing for settlement of old disputes pending under the Customs laws, the Development of Enterprise and Service Hubs (**DESH**) Bill proposed to replace the prevalent Special Economic Zones law, amongst others.

Major announcements on the tax front are expected in the comprehensive budget to be announced later this year post the elections. For the corporate sector, it is expected that the government will want to boost employment and certain tax incentives can be expected to be provided to employers. In order to increase India’s ranking on the ease of doing business, the rationalisation of withholding tax provisions, further simplification of the tax laws, and reduction in the huge backlog of litigation by way of announcement of tax amnesty schemes are certain developments that may be in the anvil. For the individual taxpayers, the government is expected to further reduce the tax rates or increase the deductions thereby resulting in more funds being available in the hands of the individuals and resulting in greater consumption. From an indirect tax perspective, various sectors will anticipate reduction in the applicable rates of Customs Duty and GST. Further, a mechanism for large taxpayers to pay the applicable GST on goods/services received from non-compliant vendors directly to the government rather than to the vendors is also likely to be introduced in the coming budget. Whether such a mechanism will in fact be beneficial to the taxpayers remains to be seen.