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Key Recommendations for Union Budget 2018: NASSCOM Submission

The IT industry has grown six-fold in revenue terms over a decade and continues to be the largest private sector employer in the organized sector.

a. IT spending is increasing globally, and investment in Global capability centres in India continues to grow.

b. The industry employs nearly 3.9 million people directly, 10 million people indirectly

c. We are already over USD100 Billion in exports, with a total share almost 50 % in service exports. We hope to cross the USD 150 Billion revenue mark this year.

d. As partners in the digital transformation for global businesses, with over 700 ODCs across 80 countries, much needs to be done for realization of its potential, both by Industry and Government.

As per RBI Balance of Payment data (released in November 2017[1]), Services have the largest net inflow of Foreign Exchange keeping India's balance of payment positive. And 64% of this net Foreign Exchange came from the software sector between **April – June 2017 (US $17304 Million)**.

Merchandise Balance of Payment deficit between Apr – Jun was at US$41 Billion. The net inflow of FE from software services, offset over 40% of this deficit.

The competitiveness of this sector is critical for India's economy and NASSCOM recommendations for the Union Budget are focused on enabling the growth of the sector and addressing concern area. Recommendations include:

1. **Concerns on GST impacting business and operations**. Suggestions for centralized administrations and modification in place of supply rules to reduce complexities should be considered, given the practical difficulties and challenges the GST regime poses in the normal conduct of business for a B2B export driven sector. The Government is aware of critical challenges, and need for changes in the Law. Challenges for the IT sector are due to peculiarities of export led intangible output and its remote and global delivery model Single point administration, appropriate place of supply rules would be the biggest motivator for the sector as it devotes its energy to continue its global march.
2. **Secondary adjustment provision** introduced last year has led to an increase in Transfer Pricing complexities for the sector. There are ambiguities on applicability, timings and other practical issues in implementation. The deemed loan approach method adopted is unique as most other countries are moving away from it or offer additional options. We recommend that an additional option may be given to the assesse to treat the secondary adjustment either as deemed dividend or deemed loan.
3. **Reduce tax rates**
   Last year, TDS was reduced to from 10% to 2 % for payments made to call centres. The industry has been requesting for across the board reduction of TDS rate to 2%.

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[1] India's overall Balance of Payment released on Nov 8, 2017 -
- https://rbi.org.in/scripts/BS_ViewBulletin.aspx?Id=17240

We request that this provision be extended to all software transactions. Our request is driven by the fact that margins are under pressure. For small companies, margins are further reduced, and a high TDS impacts cash flow.
Income tax rate rationalization promised by the Government, in view of phasing out of tax incentives has yet to happen. We repeat our request for a roadmap for tax rate reduction in a phased manner.

4. Indian IT industry are global MNCs today. We propose that **a comprehensive review of the foreign tax credit provisions be undertaken** to ensure efficiency and ease of compliance. The time when the Foreign Tax credit law was drafted, India was an importer. Things have changed today. The law today need to be reviewed from the perspective of exporting companies, as the IT sector stands today. Indian companies operating in global environment should not be at a disadvantage just because they are leading India's economic march on the world stage. For example, provisions like carry forward of unutilized foreign taxes for a certain period of time (5 years) should be considered. – this is offered by United States, the United Kingdom, Germany etc.,.
5. **Remove cascading effect of Dividend Distribution Tax on dividend** received from foreign subsidiaries, depletes profits repatriated – At present dividend received by an Indian company is taxed at 15%. There is a subsequent dual levy of Dividend Distribution Tax on this, when it is distributed to its shareholders of the parent company in India. We suggest that the tax already paid on the dividend should be allowed to be set off against tax liability from dividend distribution tax of the parent company in India.
6. **Discriminatory treatment of Indian investors – need to rationalise.**
   a. The **long-term capital gains from sale of unlisted shares** in the hands of non-residents attracts a tax of 10% whereas it attracts a tax of 20% in the hands of residents. Needs parity.
   b. Angel investors come in at the earliest stage of the company with highest risk. Imposing Angel tax on startups has a direct impact on them as it taxes investment they have received from domestic investor. (Section 56(2)(viib) of the income tax act) Startups have no revenues or profits and their valuation is based on the potential and promise of the idea, the background and competence of the founding team, etc. and is usually a matter of negotiation between the founders and the angel investors. It is often wrong for one party or the other but it is simply impossible to create a frozen logic for such investments, be it DCF or a valuation by merchant bankers, etc. As this section only applies to domestic investors, it discriminates against them as compared to foreign investors, who are not subject to this clause.
   c. While certified startups under startup India action plan have been exempted, we recommend - DIPP may certify/accredit angel groups based on specified norms and conditions in the same way that has been done for Startups and Investments made by these recognized/accredited angel groups should be exempted from this section. Suitable safeguards may be built-in to enable this.
   d. Government's commitment to strengthen the start-up ecosystem is welcome. With third largest start up community globally, India needs targeted interventions for start-ups -

i. In line with Income tax exemption, it is only fair to **offer MAT exemption to start-ups** under the start-up India action plan.
ii. **Holding period for investment to qualify as LTCG** in case of angel investors should be **reduced from the current 2 years to 1 year**. Early exits are a norm for investors in early stages. This needs to be supported.
iii. **Long term cap gains (LTCG) and short term capital gains (STCG) applicable to angel investor as compared to listed securities need harmonisation**. We recommend security transaction tax (STT) be applicable to all LTCG. For short term, 15% tax on angel investments, in harmony with listed securities
iv. Carry forward provisions although amended in the last Budget still have complexities. While shareholders in the year of loss may continue to be shareholders in the year of carry forward/ set-off of loss but this requirement should not be linked to the number of shares held by them.