# *Government releases proposed roadmap to phase-out deductions under Income-tax Act*

*November 21, 2015*

## *In brief*

In his Budget Speech this year, the Finance Minister had indicated that the rate of corporate tax will be reduced from 30% to 25% over the next four years along with corresponding phase-out of exemptions and deductions. This was a step to simplify the tax laws, making them clearer and more transparent.

In a move that exemplifies the Government's continued pragmatism and unrelenting focus on economic growth, it has recently issued a Press Release outlining how and when several deductions and exemptions in the tax law will be phased out.

## *In detail*

The Government has now announced that it proposes to implement this decision in the following manner –

- Profit-linked, investment-linked and area-based deductions would be phased out for both, corporate and non-corporate taxpayers.
- Provisions having a sunset clause would not be further modified to advance/ extend the sunset date.
- For incentives that do not have a terminal date, a sunset date of 31 March 2017 would be provided, either for commencement of activity or for claim of benefit, depending on the structure of the provision in the Income-tax Act, 1961 (the Act).
- No weighted deductions will be available with effect from 1 April 2017.

Based on the aforementioned principles the Government has planned the phase-out of the various deduction provisions under the Act in the manner laid out in the table below.

| Sl. No. | Section of the Act | Proposed plan |
|---|---|---|
| 1 | Section 32 | The highest rate of depreciation is proposed to be reduced to 60% from 100% for certain blocks of assets from 1 April 2017. The rate would apply to all assets, whether old or new, covered under the relevant block of assets. |
| 2 | Section 35AD | No weighted deduction would be allowed with effect from 1 April 2017 on any specified business which currently enjoys deduction of –<br>a. 100% on capital expenditure (other than expenditure on land, goodwill and financial asset) incurred while laying and operating a cross-country natural gas or crude or petroleum oil pipeline network, building hotel (two-star and above), warehousing facility for sugar, etc.<br>b. 150% on capital expenditure in case of cold chain facility, warehousing facility for storage of agricultural produce, and affordable housing project, production of fertilizer, etc. |

| Sl. No. | Section of the Act | Proposed plan |
|---|---|---|
| 3 | Section 35AC | No deduction will be available from financial year (FY) 2017-18 (assessment year 2018-19) in respect of expenditure on eligible projects that promote social and economic welfare. |
| 4 | Section 35 | The section provides for deduction for both, capital and revenue expenditure, and weighted deduction for donations made to certain institutions/ associations/ company incurred on scientific research. It is proposed that –<br>a. deduction under sections 35(1)(ii), (iia), (iii) and 35(2AA) be restricted to 100% from FY 2017-18, and<br>b. deduction under section 35(2AB) be limited to 100% from FY 2017-18 as against 200% available upto 31 March 2017. |
| 5 | Incentives with no sunset clause for commencement of activity | Sunset date of 31 March 2017 for commencement of activity is proposed for –<br>a. Development, operation and maintenance of infrastructure facility [Section 80-IA(4)(i)]<br>b. Development of special economic zone (SEZ) [Section 80-IAB]<br>c. Export of articles or things or services by a unit located in SEZ [Section 10AA]<br>d. Commercial production of natural gas in blocks licensed under CBM-IV and NELP VIII [Section 80-IB(9)(iv) & (v)]<br>e. Commercial production of mineral oil from block licensed under a contract awarded up to 31 March 2011 [Section 80-IB(9)(ii)] |
| 6 | Sections 35CCC and 35CCD | No weighted deduction will be available from 1 April 2017, but deduction up to 100% of the expenditure on notified agricultural extension projects and skill development projects respectively, shall be available. |

The Government has invited comments on the above proposed phase-out plan, to be sent within 15 days to the Director (TPL III) of the Central Board of Direct Taxes.

## The takeaways

- It remains to be seen whether the promised tax rate reduction takes effect from FY 2017-18 itself, when most of the exemptions/ deductions will be phased out.
- With elimination in deductions and exemptions, the difference between taxable income and book profits is bound to reduce. Further, the difference in the tax rates and the effective rate at which Minimum Alternate Tax (MAT) is levied is set to shrink even further. It is therefore an appropriate moment at which to consider removal of MAT altogether, which can be a major simplification in the tax law that can have a positive impact on investor sentiment with minimal revenue sacrifice.
- It also remains to be seen what effect the elimination of incentives to high-priority sectors will have on the stated objective of attracting foreign capital to drive India's investment-led economic growth.

## Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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