

The Digital Budget



On 8th November 2016, Indian Prime Minister announced the demonetisation of high-currency notes followed by an extensive campaign on digital payments and less-cash economy. Then on 1st February 2017, Union Finance Minister presented the Union Budget for 2017-18 at the Parliament in the backdrop of demonetisation, whose theme was TEC India, i.e. Transform | Energise | Clean India. He announced several announcements that will facilitate implementation of less-cash economy, while using the word *digital* 25 times during his Budget Speech. Then, the Finance Minister has also announced some significant changes to the provisions of the Income-tax Act, 1961 promoting the digital payments. In this article, the author aims to take up this issue and analyse the impact of these provisions. Read on...

#BudgetforAll

"India is now on the cusp of a massive digital revolution": Mr. Arun Jaitley

8th November 2016: The Government announced demonetisation of high-currency notes followed by extensive campaign on digital payments and less-cash economy.

1st February 2017: The Finance Minister stood at the Parliament, while the nation waited the unfolding of the Budget 2017 in the backdrop of

demonetisation, with a bated breath. The theme of the Budget 2017 was *TEC India*, i.e. Transform | Energise | Clean India.

In Budget 2017, the Finance Minister (FM) declared several announcements which will facilitate implementation of *less-cash* economy. He used the word *digital* 25 times during his Budget Speech. The FM has announced significant changes to the provisions of Income-tax Act, 1961 (Act) promoting digital payments. Let us analyse the impact of these provisions.



CA. Ameya Kunte

(The author is a member of the Institute who may be contacted at ameyakunte@gmail.com.)

1. Tightening screws on cash transactions – revenue and capital expenditure

Section impacted: 40A, 43 and 35D

1.1. Amendment for revenue expense:

1.1.1. Amendments proposed are as below:

- Payments otherwise than by an account

Union Budget 2017-18 [Direct Tax]

payee cheque/bank draft or use of electronic clearing system through a bank account ("cash payments") above ₹10,000 to a person in a day, shall not be allowed as deduction in computing business income. The limit has been reduced from the existing threshold of ₹20,000.

- Deeming a payment as profits and gains of business or profession if the expenditure is incurred in a year but cash payment is made in any subsequent year of a sum exceeding ₹10,000 to a person in a single day;
 - Expand the specified mode of payment under Section 40A to payment by using electronic clearing system through a bank account.
- 1.1.2. The amendment will take effect from AY 2018-19 which means the FY 2017-18.
- 1.1.3. Higher limit for cash expenditure of ₹35,000 for payments in respect of plying, hiring or leasing of goods carriage remains unchanged.
- 1.1.4. Rule 6DD of the Income Tax Rules prescribes situations where monetary threshold of incurring cash expenditure does not apply. These exceptions will continue to apply even regarding reduced limit of ₹10,000. Some of the situations covered under Rule 6DD include for example payment by debit or credit card or where the payment is made by way of adjustment against the amount of any liability incurred by the payee for any goods supplied or services rendered by the assessee to such payee.
- 1.1.5. The amendment relating to expansion of specified mode of payment under Section 40A to payment by using electronic clearing system through a bank account is welcome. While it was earlier covered by the Rule 6DD, now electronic clearing system has been introduced in the main Section itself.
- 1.1.6. Courts have considered factual situations and constraints in interpreting cash payment situations and interpretation of Section 40A(3) read with Rule 6DD. The Gujarat HC in *Anupam Teleservices* [TS-52-HC-2014(GUJ)] allowed business expediency exception to Section 40A(3) and deleted disallowance for cash payment during AY 2006-07. The Delhi High Court in *R.C.Goel.*

Rule 6DD of the Income Tax Rules prescribes situations where monetary threshold of incurring cash expenditure does not apply. These exceptions will continue to apply even regarding reduced limit of ₹10,000.

[TS-890-HC-2012(DEL)] allowed deduction in AY 2008-09, with regard to cash expenditure more than ₹20,000 in view of "business expediency" of payment under Rule 6DD(k). However, Mumbai ITAT in a recent judgment upheld disallowance in case of the assessee (engaged in shipping business) for making cash payments exceeding the prescribed limit during AY 2009-10. ITAT rejected the assessee's submission that considering the business exigencies, the payments exceeded the monetary limit and since the genuineness of purchases was established, the disallowance was not warranted.

These general principles will continue to be relevant post Budget 2017 amendment.

- 1.2. Amendment for capital expense:
- 1.2.1. It is proposed to amend the provisions of Section 43 to provide that where an assessee incurs any expenditure for acquisition of any asset in respect which a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque/bank draft or use of electronic clearing system through a bank account, exceeds ₹10,000, such expenditure shall be ignored for the purposes of determination of actual cost of such asset.
- 1.2.2. It is further proposed to amend the Section 35AD to provide that cash expenses more than ₹10,000, are not eligible for investment-linked deduction.
- 1.2.3. Rule 6DD exceptions have not been proposed to be extended in respect of capital expenditure. For example, in case of capital asset purchase by credit card, actual cost of asset will be ignored & thus, depreciation will not be available on such asset. Another situation would be introduction of capital asset in the firm by partner. This would create a disharmony in revenue and capital expenditure. Accordingly, it is suggested that the Government should consider extending the Rule 6DD relaxations even in respect of capital expenditure.

Union Budget 2017-18 [Direct Tax]

2. Measures for promoting digital payments in case of small unorganised businesses

Section impacted: 44AD

- 2.1. To boost digital economy and to encourage small unorganised business to accept digital payments, it is proposed to amend the Section 44AD to reduce the existing rate of deemed total profit of 8% to 6%. This reduced rate is applicable in respect of the amount of such total turnover or gross receipts received by an account payee cheque/bank draft/use of electronic clearing system through a bank account during the previous year or before the due date specified in the Section 139(1) in respect of that previous year. However, the existing rate of deemed profit of 8% referred to in the Section 44AD, shall continue to apply in respect of total turnover or gross receipts received in any other mode, i.e. cash receipts. The Section 44AD is available to assessee being an individual, HUF or a partnership firm other than LLP, carrying on any business other than transportation, agency, brokerage and commission) and having a turnover of ₹2 crore or less.
- 2.2. This amendment is applicable from AY 2017-18. Thus, the benefit of reduced tax is available even for current financial year 2016-17. This proposal affirms the Press Release dated 19th December 2016 citing the Government's intention to provide tax incentives.
- 2.3. Assuming a taxpayer earning ₹1 crore of income by banking channels. His deemed income @8% would have been ₹8 lakh which will now reduce to ₹6 lakh. Applying tax rates due for FY 2016-17, this results in tax saving of ₹41,200 per year.
- 2.4. A taxpayer will need to segregate the *digital/bank* turnover and cash turnover. Further, the reduced rate of 6% is not available in respect of income by way of *book adjustment* passed by way of journal entries.
- 2.5. Further, the proposed Section states that the for outstanding debtors as at 31st March, the money should be received through banking/digital models before the due date of filing of return. Thus, if a debtor remains unpaid up to the due date of filing of tax return (i.e. 31st July, 30th September or 30th November), the deemed profit would be at 8% & not 6%, even

if subsequently the amount is received by the banking/ digital modes.

Assessees availing presumptive scheme under Section 44AD must comply with the provisions of Section 269ST as also provisions of Section 206C (Tax collection at source) while accepting cash payments/advances from customers.

3. Cash transactions vertex at ₹3 lakh:

3.1. Newly introduced Section 269ST

- 3.1.1. The Finance Bill, 2017 proposes to insert the new Section 269ST, which provides that no person shall receive an amount of 3 lakh rupees or more,—
 - (a) in aggregate from a person in a day;
 - (b) in respect of a single transaction; or
 - (c) in respect of transactions relating to one event or occasion from a person, otherwise than by an account payee cheque or account payee bank draft or electronic clearing system through a bank account.
- 3.1.2. It is further proposed to provide that the restriction shall not apply to the Government, any banking company, post office savings bank or co-operative bank. Further, it is proposed that such other persons or class of persons or receipts may be notified by the Central Government, for reasons to be recorded in writing, on whom the proposed restriction on cash transactions shall not apply.

3.2. Circumvent Section 269ST, fall into the clutches of 100% penalty under Section 271DA

- 3.2.1. A new Section 271DA has been proposed, to impose a penalty on a person who receives a sum in contravention of the new Section 269ST. The penalty is proposed to be equal to the amount of such receipt, i.e. 100%. However, on a substantiated good reasoning such penalty shall not be imposed. Further, it is also proposed to subsequently amend the Section 206C to omit the provisions relating to tax collection at source at the rate of 1% of sale consideration on cash sale of jewellery exceeding ₹5 lakh.

A new Section 271DA has been proposed, to impose a penalty on a person who receives a sum in contravention of the new Section 269ST. The penalty is proposed to be equal to the amount of such receipt, i.e. 100%.

Union Budget 2017-18 [Direct Tax]

- 3.3. The provisions restricting cash transactions exceeding ₹3 lakh have been incorporated pursuant to the recommendations of the SIT constituted by the Government.

4. Electoral funding: No more Opaque

Section impacted: 13A

- 4.1. Through the Budget 2017, amendment has been proposed to the provisions of Section 13A to provide for additional conditions to avail the benefit:
- Donations of ₹2,000 or more in cash (i.e. otherwise than by an account payee cheque drawn on a bank or an account payee bank draft or use of electronic clearing system through a bank account or through electoral bonds) are prohibited;
 - Political party furnishes return in accordance with the Section 139(4B) on or before the specified due date; and
 - Further, to address the concern of anonymity of the donors, it is proposed to provide that the political parties shall not be required to furnish the name and address of the donors who contribute by way of electoral bond.
- 4.2. These amendments shall apply from the financial year beginning from FY 2017-18.
- 4.3. The Budget 2017 has reduced the limit for maintaining the details of donors from ₹20,000 to ₹2,000. This proposal along with a ban on donation exceeding ₹2,000 (discussed later) will considerably bring down the possibility of routing black money for the political funding.
- 4.4. Recently, in Common Cause [TS-22-SC-2017] ruling, the Supreme Court held that the political parties have to file the return of income and the Government should appoint an enquiring body to monitor compliance. Ramification of such ruling is thereby validated by the Finance Bill, 2017.
- 4.5. Let us assume if a political party accepts donation in cash exceeding ₹2,000 even in a single case, it would lose the exemption under Section 13A for the relevant year. Considering the wordings of Section 13A, the eligibility is to be tested for each assessment year separately. Thus, such political party (in our example), will not lose tax-exemption perpetually, but only for the relevant year.
- 4.6. Then, there are few interesting court rulings

Then, there are few interesting court rulings rendered in the last one year, which deal with tax exemption to political parties. The Delhi High Court had denied tax exemption to Indian National Congress (INC) [TS-5167-HC-2016(DELHI)-O], for AY 1994-95, for flouting audit report conditionality.

rendered in the last one year, which deal with tax exemption to political parties. The Delhi High Court had denied tax exemption to Indian National Congress (INC) [TS-5167-HC-2016(DELHI)-O], for AY 1994-95, for flouting audit report conditionality. Janata Party was similarly denied exemption for violating Section 13A conditions [TS-5169-HC-2016(DELHI)-O]. Separately, the Supreme Court vide order dated 11th January 2017 dismissed a writ petition with a plea to declare the Sections 13A and 29 of the Representation of People Act giving 100 % exemption to political parties as unconstitutional with an observation: *Political parties need public fund to project their ideologies and there is no wrong with the policy to exempt them under the Income-tax Act. It's an executive action and doesn't violate the constitution.*

5. Restrictions on cash donation

Section impacted: 80G

- 5.1. It is proposed to amend the Section 80G to provide that no deduction shall be allowed in respect of donation of any sum exceeding ₹2,000 (reduced from ₹10,000 pre-budget scenario) unless such sum is paid by any mode other than cash.
- 5.2. The amendment has been introduced in order to provide cash-less economy and transparency. The amendment shall be applicable from FY 2017-18, i.e. AY 2018-19.

Conclusion

Less-cash economy will be a reality only with a change of mindset of our fellow citizens to not using cash for day-to-day transactions. This will be possible only with consistent positive experience with banking or digital payment channels. Tax incentives in this context are a very small part of overall policy initiatives and the Government should continue to focus on building banking and digital infrastructure. ■