Union Budget 2015
Inspiring confidence, empowering change in India

Technology
Post-budget sectoral point of view
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Context

Where are we
The technology sector continues to evolve in 2015 with prioritisation on enabling transformation and taking steps towards creating a ‘Digital India’. India is one of the leaders in the global technology domain ranging from IT hardware manufacturing and software development to providing BPO and technology services to clients. According to NASSCOM\(^1\), the industry is projected to achieve revenues of USD\(146\) billion in 2015, up from USD\(118\) billion in 2014. The projection for exports in 2015 is expected to be USD\(100\) billion which is approximately 13 per cent higher than 2014.

Growth in technology services is being driven by digital solutions around Social, Mobile, Analytics and Cloud (SMAC) and other emerging areas of the ‘Internet of Things’ agenda and cyber security. Digital technology accounts for 12-14 per cent of the industry’s revenue. There is an increased demand for mobility, ERP and CRM. Main drivers for the technology sector are; greater automation and application of analytics across the entire value chain.

According to NASSCOM\(^1\), 2014 saw the emergence of 3,100 start-ups, making India the fourth largest start-up hub in the world. USA emerged as the largest market for exports. The domestic technology industry, driven by e-commerce and a stable government focus on technology adoption, is projected to grow at 14 per cent in 2015 and generate a revenue of around USD\(48\) billion.

Key issues/challenges
With the increased focus of the government on the technology sector, there are a few challenges the sector faces including stiff competition from other Asian and emerging economies, data security and inadequate infrastructure. The lack of infrastructure pushes start-ups to take on offers from foreign companies.

What was expected
The Finance Minister held pre-budget discussions with CEOs of various e-commerce companies and start-ups, both in the software and the hardware space. This forum addressed topics which include the contribution of IT to ‘Make in India’, regulatory and tax challenges of technology start-ups and SMEs. These initiatives emphasise the importance given by the government to the campaigns: ‘Digital India’ and ‘Make in India’. However, greater clarity was sought on the contribution of the two campaigns. Also, the government was expected to invest a substantial amount of money to develop a robust network of infrastructure across the country. A major expectation from the budget was that there will be clarity on the taxation of e-commerce companies. Key pre-budget recommendations for the sector included providing funding and incentives to start-ups and SMEs for them to support operations and stable policies and regulations for large enterprises.

1. NASSCOM Strategic Report published in Feb, 2015
Key announcements

• The Indian government has set aside INR1000 crores to set up a Self-Employment and Talent Utilisation (SETU) programme that will help incubate start-ups, especially in the technology sector. The techno-financial incubation and facilitation programme will aim to create over 1,00,000 jobs and significant revenue.

• The government will set up the Atal Innovation Mission with an initial fund of INR150 crores for research and development to provide a network of leading hubs. With the help of entrepreneurs and researchers, the platform aims to foster a culture of innovation and research and development.

• Indian Railways is expected to invest in the technology sector to provide better facilities to passengers like, e-catering in 108 trains, open Wi-Fi facilities at 400 stations, Hand-held terminals for Travelling ticket examiners.
**Tax proposals**

**Direct tax proposals**

- Reduction in headline corporate tax rate over the next four years from 30 to 25 per cent, while phasing out of industry-specific exemptions

- Effective 1 April 2015 (FY 2015-16), the rate of surcharge on the income-tax of domestic companies has been increased from:
  - Five to Seven per cent for income exceeding INR10 million and up to INR100 million; and
  - 10 to 12 per cent for income exceeding INR100 million.

- Clarity relating to taxation of indirect transfer provisions proposed with a view to create a favourable investment planet. Rules for computation mechanism to be prescribed

- General Anti-Avoidance Rule (‘GAAR’) could be made applicable from FY 2017-18 onwards. Investments made up to 31 March 2017 to be protected from the applicability of GAAR

- To facilitate technology inflow to small businesses at low cost, rate of tax on royalty and FTS payments made to non-residents reduced from 25 to 10 per cent

- Any company would be regarded as being a tax resident of India if its place of effective management, at any time in that year, is in India

- Proposal to provide tax pass through status to Category-I and II alternative investment funds for encouraging infusion of private equity in to start-ups

- Threshold for applicability of domestic transfer pricing provisions enhanced from INR50 million to INR200 million.

IT manufacturing companies and software product companies can be impacted by the following proposals:

- Allowability of 50 per cent of additional depreciation on new plant and machinery acquired by manufacturing entities and used for less than 180 days in the immediately succeeding financial year

- To generate greater employment opportunities, the threshold limit of minimum number of new regular workmen under Section 80JJA of the Act reduced from 100 to 50

- Incentivising the manufacturing sector in the notified backward areas of Andhra Pradesh and Telangana through:
  - provision of additional investment allowance at 15 per cent of cost of new assets installed; and
  - provision of additional depreciation at 35 per cent of cost of new plant and machinery installed

Increased focus on tax compliance with more stringent penalties/consequences:

- Employers to collect information/proof in a prescribed form before allowing exemptions to employees while deducting tax at source

- Indian companies to provide information of indirect transfer affecting it; and

- Information of payment to non-residents to be provided, whether or not chargeable to tax.
**Indirect tax proposals**

**Service tax [proposals effective from notified date]**
- Service tax rate has been increased from 12.36 per cent to 14 per cent in line with the expected GST rate; Education Cess and Secondary and Higher Education Cess is to be subsumed
- Additionally, ‘Swachh Bharat’ cess of two per cent may be imposed on all or any of the taxable services
- Effective 1 April 2015:
  - manpower supply and security services by non-corporates to companies will now attract 100 per cent of service tax under reverse charge as against partial reverse charge.
  - CENVAT Credit on partial reverse charge mechanism is now allowed on payment of service tax without linking it to the payment towards value of service.

**Excise duty [proposals effective from 1 April 2015]**
- Excise Duty rate has been increased from 12 to 12.5 per cent; Education Cess and Secondary Higher Education Cess on all goods has been withdrawn
- Tablet manufactures have an option to pay two per cent excise duty without CENVAT credit or 12.5 per cent with CENVAT credit.

**Customs [proposals effective from 1 March 2015]**
- Due to an increase in Excise Duty rate from 12 to 12.5 per cent, the effective Customs Duty rate will marginally increase; Cess on Basic Customs Duty will however continue to be the same
- Full exemption from SAD on all goods except, populated Printed Circuit Boards (PCB) used in the manufacture of Information Technology Agreement (ITA) Bound Items
- Full exemption of import duties on parts, components and accessories sourced manufacture of tablet computers and their sub-parts.

**Others**
- Penal provisions amended with an aim to reduce litigation
- Facility of advance ruling is being extended to all resident firms
- Central excise/Service tax registrants are allowed to use digitally signed invoices and maintain records electronically
- Time limit for taking CENVAT credit on inputs and input services increased from six months to one year
- Speedier online process for Service tax and Excise registrations.

**Regulatory proposals**

The Union Budget 2015 also contains certain proposals regarding financial markets which may, inter alia, impact the technology sector. One such proposal is to recognise Capital Account Controls as being a policy, rather than a regulatory matter. Amendments are therefore being proposed in the Foreign Exchange Management Act, 1999, to provide control on capital flows as equity will be exercised by the Central Government, in consultation with the Reserve Bank of India.

Consequently, the Regulations that have currently been issued by the RBI, inter alia, on foreign direct investments, outbound investments, borrowing loans in foreign exchange, setting-up of branches in India by foreign companies shall continue to be valid, until amended/rescinded by the Central Government.
Impact

An investment of INR100 million by the government in SETU is heartening. This will help start-ups overcome their financial issues. The multiple technology initiatives taken in the Railway sector can popularise the ‘Digital India’ campaign.

Government’s imprint on growth, infrastructure, job creation and skill development will have a positive impact on the technology sector. The additional outlay for IT start-ups, fully IT-based scholarships, and harmonising the efforts on skill development through the National Skills Mission will extend necessary funding and skill support to the sector. There will be additional spend on setting up leading technology and management institutes.

The intention is to move from an exemption-based system to an internationally competitive tax regime, over the next four years with certainty, transparency and stability. Reduction in the rate of tax on royalty/FTS payments to non residents from 25 to 10 per cent is expected to facilitate technology inflow.

The budget proposals seek to simply indirect tax procedures. With the vision of incentivising domestic manufacture and impetus being given to ‘Make in India’, the Hardware sector is expected to benefit due to the exemption from SAD on all goods except PCBs used in the manufacture of ITA bound items. However, the increase in rate of excise duty and service tax can adversely impact the software sector.
Unfinished agenda

What remains

- Greater clarity was required on the contribution of the technology sector in the two campaigns: ‘Digital India’ and ‘Make in India’
- Issue of dual levy of VAT and service tax on software products
- Rationalisation of minimum alternative tax and dividend distribution tax for SEZ activities
- Extending weighted R&D deduction for companies providing software services
- Tax impetus for building infrastructure for large data centres and cloud services within the country
- Investments by angel investors in start-ups over its fair market value not to be taxed.

What is expected going forward

- Clarity on taxation of e-commerce transactions and software payments as royalty
- Provision of tax impetus for digitisation of SMEs
- Building a policy framework for SMEs in the technology sector to facilitate innovation
- Point of view of the IT ministry on ‘smart cities’.
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