



## Union Budget 2022 – Key proposals impacting the life sciences and health care industry

The Finance Bill, 2022 has proposed amendments to income-tax provisions on deductibility of expenses and withholding tax. These amendments are likely to have a significant impact on the life sciences and health care industry.



### Proposed amendment to Section 37

It is clarified that deduction will not be allowed for:

- Providing any benefit or perquisite to a person where acceptance of such benefit or perquisite violates any law, rule, regulation, guideline governing conduct of such person, or
- Expenditure incurred for a purpose that is an offence under any law or for compounding an offence under any law, enforced in India or outside India



### Proposed insertion of Section 194R

Withholding tax obligation cast on a person responsible for providing to a resident, any benefit or perquisite, whether convertible into money or not

Proposed withholding tax rate: 10 percent of the value or aggregate of value of such benefit or perquisite

# Proposed amendment to S.37

## I. Expenses towards the benefit or perquisite, acceptance of which, violates any law

### Background

The deductibility of expenses incurred by pharmaceutical companies towards travel, hospitality, conference expenses, etc., of doctors has been a litigious issue.

The Central Board of Direct Taxes had noted that regulations issued by the Indian Medical Council (IMC) prohibits medical practitioners from accepting any gifts or benefits (as prescribed) from the pharmaceutical and allied health sector industries. It issued a circular (no. 5 of 2012) directing inadmissibility of expenses incurred in providing freebies to medical practitioners.

Tribunals have generally allowed the expenditure— primarily on the basis that IMC regulations apply to the medical professionals and not to pharmaceutical

companies. However, recently the Supreme Court has held against the taxpayer on the basis that freebies provided to doctors are prohibited by law and therefore, should not be allowed a deduction to the pharma companies providing such freebies

### Snapshot of the proposed amendment

The Union Budget 2022 proposal seeks to disallow some of these expenses, to the extent where it results in a benefit or perquisite for the recipient and is in violation of any law, rule, regulation, or guideline governing the conduct of such recipient.

### Impact of the proposed amendment

- Potential disallowance and consequent impact on effective tax rate/provisioning/penalty
- Potential interplay with GST provisions; consistency of tax positions across income-tax and GST

## Potential impact areas



### Key areas for detailed examination, vis-à-vis deductibility

- Nature and purpose of the expense
- Whether a benefit or a perquisite accrues to the recipient
- Law/regulations governing the recipient
- Documentation to substantiate the claim
- Interplay with prevailing jurisprudence
- Impact of the recent Supreme Court judgement including impact on historic litigation especially where favorable decisions were upheld by lower appellate authorities
- Impact from a governance perspective, including for alternate arrangements
- Audit provisioning
- Applicability: retrospective or prospective

### Key areas for detailed examination, vis-à-vis GST

- Re-evaluation of character of such expense with guidelines
- Input tax credit restrictions for the company, in case the benefit is recognised as gifts
- Establishing a nexus of expenses with business operations of the company
- "Violation of law" to be considered for input tax credit availment
- Change in GST credit availment process for such expenses
- Impact on GST cost incurred for sales promotion expenses
- Presence of appropriate documentation to prepare from an audit-readiness perspective
- Impact on past input tax credit, availed by company prevailing jurisprudence

## II. Expenses for compounding of an offence or an act prohibited by any law, including foreign law

### Background

There was some ambiguity as to whether expenses incurred for a purpose that is an offence under foreign law or for compounding of an offence for violation of foreign law is inadmissible for income-tax purpose. Taxpayers contended that the S. 37 provisions apply only to offences that are prohibited by the domestic law of the country.

### Snapshot of the proposed amendment

Expenditure shall be inadmissible if it is incurred for a purpose that is an offence under any law enforced in India or outside India; or for compounding an offence under any law enforced in India or outside India.

### Key impact of the proposed amendment

- Determination of expense incurred for a purpose that is an offence under any foreign law
- Cost of compounding violation of foreign laws
- Amounts incurred to settle disputes between parties, in case of violation of laws, e.g., infringement of intellectual property rights



# Proposed introduction of S. 194R

## Snapshot of the proposed amendment

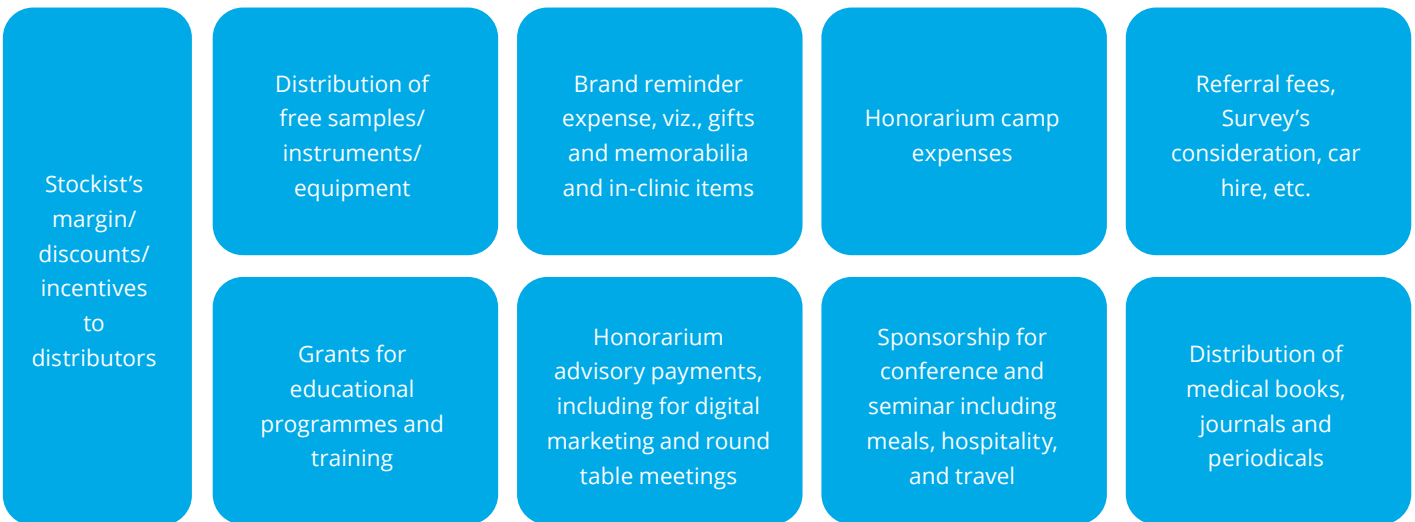
Provision of benefits or a perquisite exceeding INR 20,000 to a resident during a financial year (during business or profession) to be subject to withholding tax at the rate of 10 percent.

Where cash portion is inadequate to cover the withholding tax liability, the provider of the benefit or perquisite needs to ensure that the tax has been paid by the recipient of the benefit or perquisite.

## Impact of the proposed amendment

- Potential withholding tax obligation/implications of not undertaking tax withholding
- Increase in cost, if tax is to be borne by the company providing the benefit or perquisite
- Multiple layer withholding
- Appropriate mechanism to discharge tax
- Potential interplay with GST provisions; consistency of tax positions across income-tax and GST

## Potential impact areas



### Key areas for detailed examination, vis-à-vis withholding tax obligation

- Nature and purpose of the expense
- Whether a benefit or a perquisite accrues to the recipient
- Interplay with prevailing jurisprudence
- Interplay with other withholding tax provisions

### Key areas for detailed examination, vis-à-vis GST

- Transactions characterized as gifts could have input tax credit restrictions for the company
- Benefit/perquisite TDS deduction under the proposed amendment would require a detailed evaluation on whether it qualifies as "supply" under GST law or not
- Transactions regarded as indirect sales promotion could have GST implication
- Assessments based on withholding tax (194R) data from business partners
- Principles of Circular 105/24/2019 - GST (rescinded) could be made applicable for determining GST liability
- Assessment of additional GST cost, if any, in overall supply chain



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