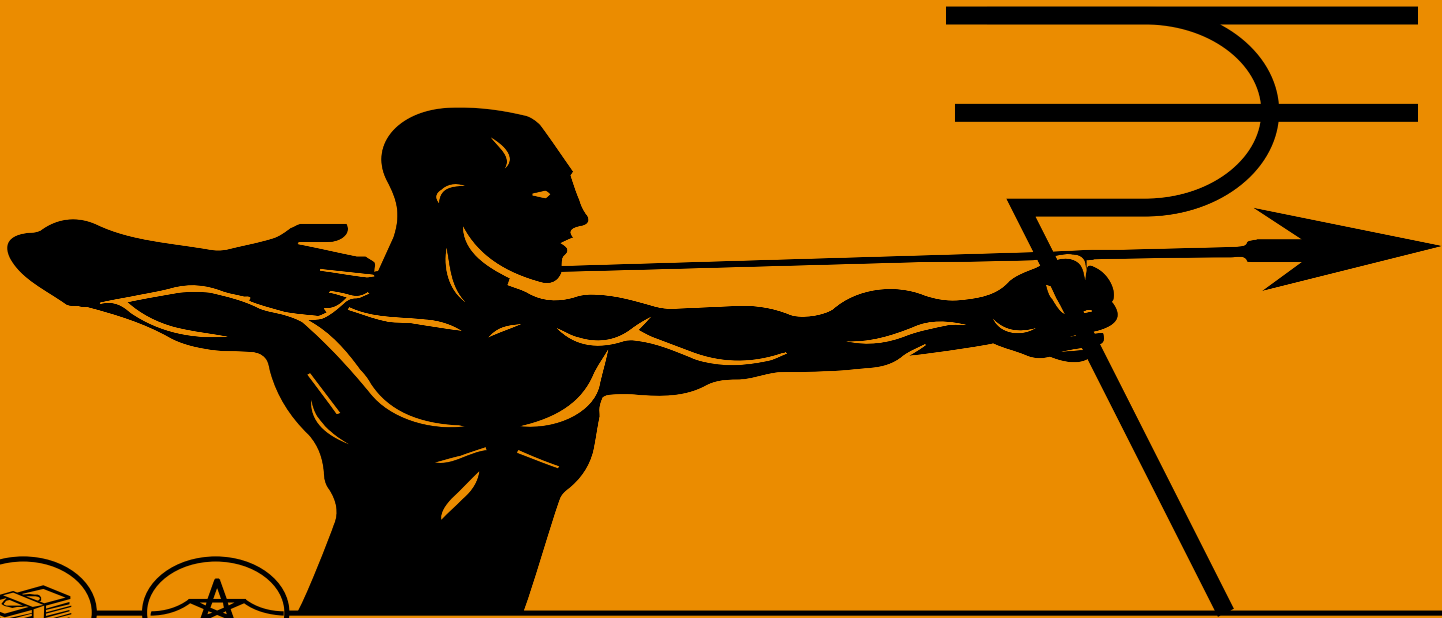
Union Budget 2018

Aiming for the bullseye



Financial services

Key proposals

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Budget 2018 – General tax and Regulatory

General tax and Regulatory | Banking and Capital markets | Private equity and VCs | Real estate and Infrastructure | Insurance and Asset Management | Others

Key policy announcements

Foreign Exchange Laws

- Proposal to review existing regulations for developing an integrated Overseas Direct Investment policy

Fintech

- Policy and institutional development measures to be examined for the growth of Fintech companies in India
- National program to be initiated to direct efforts in the area of Artificial Intelligence, including research and development of its applications
- Blockchain technology to be explored proactively for ushering in a digital economy
- Measures expected to eliminate use of crypto-assets in financing illegitimate activities or as part of the payment system

Others

- Review of MUDRA's policy and eligibility criteria for refinancing of NBFCs
- Introduction of scheme to assign every individual enterprise in India a unique ID similar to Aadhaar
- Stamp duty regime for financial securities transactions to be reformed
- Gold Policy to be formulated to develop gold as an asset class. Gold Monetisation Scheme to be revamped to enable people to open a hassle-free Gold Deposit Account
- Agri-Market Infrastructure Fund with a corpus of INR 20 billion to be set up for developing and upgrading agricultural marketing infrastructure

Key regulatory proposals

- RBI empowered to accept deposits for liquidity management under the Standing Deposit Facility Scheme

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Budget 2018 – General tax and Regulatory

General tax and Regulatory | Banking and Capital markets | Private equity and VCs | Real estate and Infrastructure | Insurance and Asset Management | Others

Key direct tax proposals

Tax rates - Corporates

- Benefit of lower tax rate of 25% (excluding surcharge and cess) extended to domestic companies having total turnover/gross receipts up to INR 2,500 million during financial year (FY) 2016-17; tax rate for other companies remains unchanged

Tax rates - Others

- No change in the income-tax slabs/rate and surcharge on income-tax for others
- Education cess of 3% to be replaced with Health and Education cess of 4%

Implications of non-filing of tax return (FY 2017-18 onwards)

- Non-filing of tax returns by corporates to entail prosecution implications without any monetary threshold of tax payable

Standard deduction for salaried tax payer

- Standard deduction of INR 40,000 introduced for salaried tax payers
- Current exemption in respect of transport allowance (except in case of differently-abled persons) and reimbursement of medical expenses is proposed to be withdrawn

Permanent Account Number (PAN) (FY 2017-18 onwards)

- PAN to act as Unique Entity Number (UEN) for non-individuals
- PAN mandatory for financial transactions exceeding INR 0.25 million in a financial year

Transfer pricing - Country-by-Country reporting (CbCR)

- Rationalisation of provisions relating to CbCR with effect from 1 April 2017 (FY 2016-17)
- Time allowed for furnishing CbCR to be extended to 12 months from the end of reporting accounting year
- Constituent Entity (CE) resident in India shall furnish CbCR, in case its parent entity outside India has no obligation to file the report
- If alternate reporting entity nominated by parent entity outside India files CbCR in its jurisdiction, within the time specified locally, then the CE resident in India is not required to furnish CbCR in India

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Budget 2018 – Banking and Capital markets

General tax and Regulatory | Banking and Capital markets | Private equity and VCs | Real estate and Infrastructure | Insurance and Asset Management | Others

Key policy announcements

- Expediting loan sanction by bank to SMEs through revamping of existing online system
- Recapitalisation to help public sector banks to grant additional credit of INR 5 trillion
- Amending SEBI Act, SCRA and Depositories Act to streamline adjudication procedures and provide for penalties for certain infractions
- Linking of public sector banks and corporates on the Trade Electronic Receivable Discounting System (TReDS) platform
- Uniform regulatory authority for financial services in IFSCs to be set up
- Government to announce measures for addressing non-performing assets and stressed accounts of MSMEs in order to enable larger financing of MSMEs and to ease cash flow challenges faced by them
- SEBI to consider mandating large corporates to meet about one fourth of their financing needs from bond market
- Strong Regional Rural Banks to be permitted to raise capital from the market to enable them to increase their credit to rural economy
- Kisan Credit Cards scheme to be extended to fisheries and animal husbandry farmers to help them meet their working capital needs

Key direct tax proposals

- Certain provisions of ICDS now codified as part of Income-tax Act (FY 2016-17 onwards)
  - RBI policy v. provisions of Income-tax Act - which one will prevail in case of conflict
  - Exceptions like uncertainty in collection of revenue - absent
  - Derivatives held by NBFCs / Stock brokers - whether to be treated as inventories as per ICDS
- Trading in agricultural commodity derivatives on recognised stock exchange, which are not chargeable to Commodity Transaction Tax (CTT), to be treated as non-speculative transactions
- Proposed levy of CTT w.e.f. 1 April 2018 as follows:

Transaction	Rate	Payable by
Sale of option on commodity derivative	0.05 %	Seller
Sale of option on commodity derivative where option is exercised	0.0001 %	Purchaser

Budget 2018 – Banking and Capital markets

Key direct tax proposals

- Brought forward losses of a company may not lapse in case of any change in shareholding which is pursuant to a resolution plan approved under Insolvency and Bankruptcy Code, 2016 (IBC), after giving a reasonable opportunity of being heard to the IT authorities (FY 2017-18 onwards)
- Aggregate of unabsorbed depreciation and brought forward losses to be allowed as a deduction while computing book profits under MAT provisions for companies where corporate insolvency resolution has been admitted under IBC (FY 2017-18 onwards)
- Return of Income filed by companies whose application for corporate insolvency resolution has been admitted under IBC should be verified by insolvency professional (applicable for filings made on or after 1 April 2018)

Proposal relating to International Financial Service Centre (IFSC)

- Rate of Alternate Minimum Tax (AMT) applicable to non-corporate entities operating in IFSC reduced to 9% (from 18.5% applicable earlier)
- Capital gains on transfer of following securities by a non-resident on a recognised stock exchange in IFSC exempted from income-tax:
  - Bonds and GDRs;
  - Rupee denominated bonds, and
  - Derivatives

Key regulatory proposals

- Penal provisions introduced under the SEBI Act, to apply in case of failure to comply with the Investment Adviser or Research Analyst Regulations or any direction(s) issued by SEBI thereunder:
  - Minimum Penalty - INR 0.1 million
  - Maximum Penalty - INR 0.1 million per day till non-compliance subsist (subject to upper cap of INR 10 million)

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Budget 2018 – Private equity and VCs

Key Policy announcements

- Policy for permitting foreign investment in hybrid instruments of startups and venture capital firms to be rolled out
- Additional measures to strengthen the environment for growth and successful operation of AIFs in India to be undertaken

Key regulatory proposals

Penal provisions for non-compliance with securities law

- Penal provisions introduced under the SEBI Act to apply in case of failure to comply with the AIF / REIT / InvIT Regulations or any direction(s) issued by SEBI thereunder:
  - Minimum Penalty - INR 0.1 million
  - Maximum Penalty - Higher of (i) INR 0.1 million per day till non-compliance subsist (subject to upper cap of INR 10 million); or (ii) 3 times the amount of gains made due to non-compliance
- Penaltly of upto INR 250 million shall be levied on any person managing the AIF / REIT / InvIT for failure to comply / breach of the listing and delisting conditions under the SCRA Act

Key direct tax proposals

Incentives for eligible start ups *(FY 2017-18 onwards)*

- Tax holiday benefit is now available to eligible startups incorporated prior to 1 April 2021 (earlier 1 April 2019)
- Definition of eligible business widened to include innovation, development or improvement of products or processes or services or scalable business model with high potential of employment generation or wealth creation
- Turnover of business should not exceed INR 250 million for seven years from the year of incorporation (earlier required up to FY 2020-21)

Widening the ambit of 'business connection'

- Definition to be aligned with Multilateral convention to also include a person who habitually concludes contracts or plays a principal role leading to conclusion of contracts on behalf of the non-resident though the person may not have authority to conclude contracts
- Significant economic presence of a non-resident in India shall also constitute business connection (i.e. non-residents operating through digitised businesses without any physical nexus in India)

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Budget 2018 – Private equity and VCs

General tax and Regulatory | Banking and Capital markets | Private equity and VCs | Real estate and Infrastructure | Insurance and Asset Management | Others

Key direct tax proposals

Taxation of long term capital gains

- Exemption for long term capital gains (LTCG) on Securities Transaction Tax (STT) paid transfer of listed equity shares, units of equity oriented mutual fund and units of business trust withdrawn - w.e.f. 1 April 2018
  - Impact on pre-IPO transactions
- New provision introduced for taxation of such LTCG above INR 0.1 million at the rate of 10% w.e.f. 1 April 2018
- Central Government may by notification specify the nature of acquisition of equity shares to which the condition of STT paid on acquisition shall not apply
- Computation of gains in foreign currency and indexation benefits not available
- Cost of acquisition to compute LTCG to be higher of:
  - Actual cost of acquisition; and
  - Lower of:
    - FMV (defined) as on 31 January 2018; and
    - Value of consideration received upon transfer
- The above cost step up benefit currently not provided for FPIs

Illustration:

Particulars	Situation 1	Situation 2	Situation 3	Situation 4
Acquisition of listed equity shares – 1 April 2016 **(A)**	100	100	100	100
FMV - 31 January 2018 **(B)**	140	80	80	120
Sale of listed equity shares - 1 July 2018 **(C)**	160	70	90	90
(D) = Lower of (B) and (C)	140	70	80	90
Cost of acquisition of shares as per new section 112A – **(E)** = Higher of **(A)** and **(D)**	140	100	100	100
Long term capital gain / (loss) **(F)** = **(C) - (E)**	20	(30)	(10)	(10)

Original cost protected at all times - Cost re-base can only result into lowering of tax cost

Budget 2018 – Real estate and infrastructure

Key policy announcements

- Proposal to establish Affordable Housing Fund within the National Housing Bank funded from priority sector lending shortfall and fully serviced bonds authorised by the Government of India
- Under Prime Minister Awas Scheme Rural, 5.1 million houses during FY 2018-19 will be constructed exclusively in rural areas
- National Highways Authority of India to consider organising its road assets into SPVs and use innovative monetising structures such as Toll, Operate and Transfer and InvITs

Key direct tax proposals

Taxability of conversion of inventory into capital asset

- Hitherto, taxability on conversion of stock-in-trade into capital asset was not clear in absence of express provisions
- Conversion of stock-in-trade into capital asset to now trigger taxability as business income
  - Taxability in the year of conversion and not on eventual sale – may result in immediate tax outgo on notional income
  - FMV of inventory on the date of conversion to be deemed as full value of consideration and treated as cost of acquisition of the capital asset
  - Period of holding to be reckoned from the date of conversion
- Proposed amendment likely to impact developers changing business model from build-to-sell to build-to-lease

Safe harbour provisions for transactions involving immovable property

- Deemed consideration provisions for taxation of income on transfer of immovable properties not to apply if the stamp duty value of the immovable property does not exceed the transaction value by more than 5% of the transaction value

Illustration:

Particulars	Situation 1	Situation 2
Actual sale consideration	100	100
Stamp duty value	104	110
Deemed sale consideration (Pre)	104	110
Deemed sale consideration (Post)	100	110

Revenue recognition for construction contracts/ contract of services (FY 2016-17 onwards)

- Income from construction contracts/ contract of services to be determined based on percentage of completion method as per ICDS
- Following exceptions are proposed to the above:
  - a service contract for a period of less than 90 days – income to be determined on the basis of project completion method
  - a service contract involving indeterminate number of acts over a specific period of time – income to be determined on the basis of a straight line method

Budget 2018 – Insurance

General tax and Regulatory | Banking and Capital markets | Private equity and VCs | Real estate and Infrastructure | **Insurance and Asset Management** | Others

Key policy announcements

Insurance

- National Health Protection Scheme providing cover to over 1 billion poor and vulnerable families to be launched. Each family to receive a cover up to INR 0.5 million per year for secondary and tertiary care hospitalisation
- Three public sector general insurance companies (National Insurance Company Ltd, United India Assurance Company Ltd and Oriental India Insurance Company Ltd) to be merged into one general insurance company, which will be subsequently listed
- Two public sector insurance companies proposed to be listed
- Pradhan Mantri Jan Dhan Yojana expanded to provide micro insurance services and unorganised sector pension schemes

Asset Management

- Following the success of ETF Bharat-22 introduced by the Government, the Department of Investment and Public Asset Management is expected to come up with more Exchange Traded Fund (ETF) offers including debt ETF

Key direct tax proposals

Insurance

- In case of senior citizen, being taxpayer himself or any of his family member (except parents), deduction would be available up to INR 50,000 for any payment made towards health insurance or medical treatment of such senior citizen
- For senior citizen parents, aggregate deduction for payment towards health insurance/preventive health check up or medical expenditure, would be available up to INR 50,000 as against the present limit of INR 30,000
- Deduction for health insurance premium paid in lump sum (with multi-year coverage) to be available proportionately over the period of health insurance cover

Asset Management

- Effective 1 April 2018, LTCG, in excess of INR 0.1 million, on transfer of units of Equity Oriented Fund (EOF), units of business trust taxable at the rate of 10% (provided the transfer is subject to STT)
- Definition of EOF to also include fund of funds where minimum 90% of assets are invested in listed units of other fund and such other fund in turn has invested minimum 90% in listed equity shares
- Effective from 1 April 2018, an EOF is liable to pay additional tax at the rate of 10% on the income distributed

Budget 2018 – Others

Other key direct tax proposals

Deemed Dividend

- Loans, advances and other payments deemed as dividend to now attract dividend distribution tax @ 30% (without grossing up) in the hands of the company providing such loan or advance or making such payment
  - Additional income-tax at the rate of 10% not applicable on such transactions in case of specified recipients
  - Such dividend exempt in the hands of the recipient; withholding tax on such transactions not to apply
- In case of amalgamated company, accumulated profits for deemed dividend shall be increased by accumulated profits of amalgamating company on the date of amalgamation (FY 2017-18 onwards)

Income from other sources

- Deemed income provisions shall not apply on receipt of capital assets without any, or without adequate consideration by:
  - a wholly-owned Indian subsidiary from its holding company; and
  - an Indian holding company from its wholly-owned subsidiary

Taxability on account of change in contractual terms

- Consideration received on termination or modification of contractual terms relating to business or employment (whether in the nature of revenue or capital) deemed as taxable income

Scope of capital gains exemption on investment in bonds restricted

- Capital gains exemption on investment in specified bonds restricted to capital gains arising on sale of land or building or both (exemption was earlier available on sale of any long term capital asset)
- Investment in bonds after 1 April 2018 eligible for exemption now if such bonds are redeemable after 5 years (instead of redemption after 3 years prescribed earlier)

Deduction linked to filing of tax return within due date *(FY 2017-18 onwards)*

- Deduction in respect of certain income now available only if the tax return is filed by the tax payer within the prescribed due date

Return of income *(FY 2017 -18 onwards)*

- Prima facie adjustments to total income with respect to receipts included in Form 26AS or Form 16/ Form 16A while processing of returns, not to be made for returns filed on or after 1 April 2018

E-assessment *(FY 2017 -18 onwards)*

- E-assessment proposed to be introduced to eliminate interface between assessee and tax payer; Government to notify the details of the scheme

National Pension Scheme *(NPS)*

- Withdrawal up to 40% from the NPS Trust now exempt from tax for all subscribers, not just employees

Budget 2018 – Others

General tax and Regulatory | Banking and Capital markets | Private equity and VCs | Real estate and Infrastructure | Insurance and Asset Management | Others

Other key proposals

Incentive for employee generation

- Reduced minimum period of 150 days for employment of additional employees now extended to assessees engaged in the business of manufacturing of footwear or leather products
- In cases where minimum employment period criteria of 240 / 150 days (as the case may be) is not satisfied in the relevant financial year, but is completed in the succeeding financial year, then the deduction for the additional employee cost can be claimed from the succeeding financial year in respect of such new employees

Increased penalties for non-reporting of financial transactions
(FY 2017-18 onwards)

- Enhanced penalties prescribed for non-compliance in reporting of specified financial transactions and reportable accounts (under FATCA CRS regulations)

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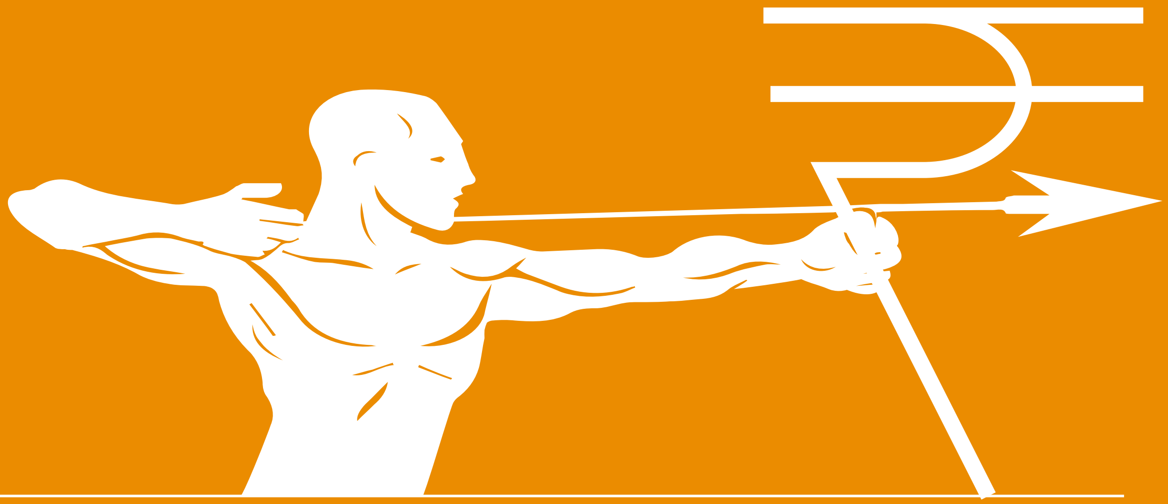

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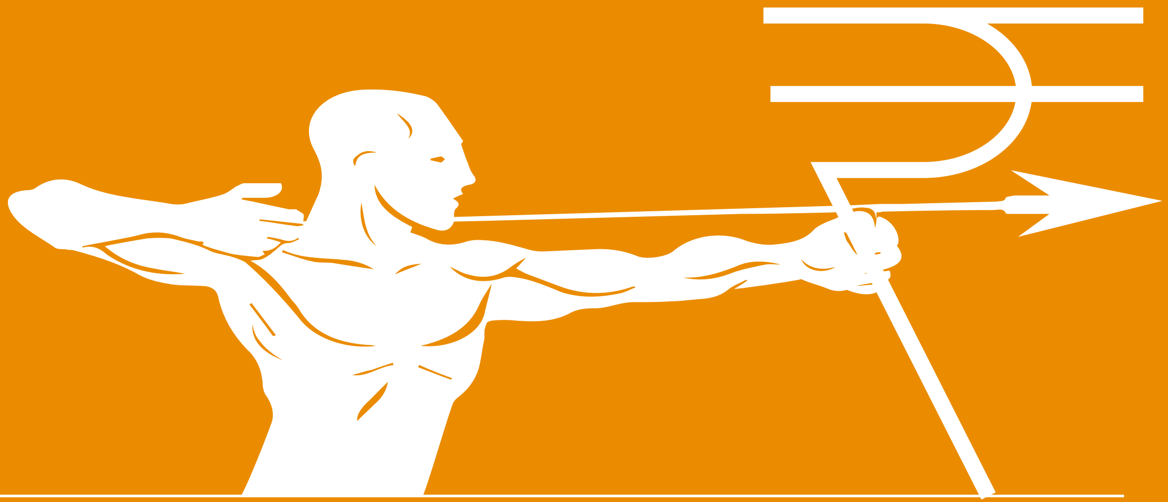

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