RESOURCE PAPER - 25

INDO-JAPAN CHAMBER OF COMMERCE & INDUSTRY

Highlights of the Union Budget 2019-2020

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PREFACE

The Indo-Japan Chamber of Commerce and Industry provides updates on important happenings in Japan and India and Japan-India related matters. This issue of Resource Paper focuses on the highlights of the Union Budget 2019-2020 of the Government of India. It would be our pleasure to provide any information required by the reader on any topic covered in this issue, as it may not be feasible to present a very detailed Budget Document. I hope the readers would find it informative.

The Authors of the Paper are Mr. R. Sridhar and Mr. Subham Kumar. Mr. Sridhar is a qualified Company Secretary and Lawyer with over 22 years post qualification experience in tax and regulatory matters. He is a TAX partner in Grant Thornton LLP where he is responsible for the tax practice of Chennai and Kochi offices. He is also responsible for the Transaction Tax practice of the firm for South India.

Grant Thornton in India is one of the largest assurance, tax, and advisory firms in India. With over 3,000 professional staff across 15 offices, the firm provides robust compliance services and growth navigation solutions on complex business and financial matters through focused practice groups. The firm has extensive experience across a range of industries, market segments, and geographical corridors

Mr. Subham Kumar is a Chartered Accountant with about 9 years of experience. He is an Associate Director with Walker Chandiok & Co. LLP and specializes in income tax and corporate reorganisations.

July 2019

Suguna Ramamoorthy
Secretary General

Highlights of the Union Budget 2019-2020

Budget 2019 Vision Towards Sustainable Growth:

The Union Budget 2019 announced by India's first full time woman Finance Minister Ms. Nirmala Sitharaman laid down the road map for India becoming a USD 5 trillion economy within the next 5 years, is in line with the vision for a USD 10 trillion economy in the forthcoming decade. The budget aims at growth in a sustained manner with focus on both urban and rural sectors. Following are the key highlights:

Organising the Global Investor Meet in India:

In a very interesting and as a bold measure with an objective to make India integral part of global financial system, the Government proposes to organize an annual Global Investors Meet in India, using National Infrastructure Investment Fund as the anchor which will invite top industrialists/corporate honchos, top pension/insurance/sovereign wealth funds and top digital technology/venture funds.

Liberalisation in FDI and measures for Industrial Development:

The Government proposed to easing local sourcing norms for single-brand retail trading by relaxing the existing 30% sourcing norms to allow group entities to source from India and / or enhance the scope or coverage. The Government also proposes to increase the FDI limit in Aviation, Insurance and Media

(Animation, Visual, Comic and Graphic) sector. Further, increasing FDI in Insurance Intermediaries sector up to 100%.

Capital Market and Financial Sector:

Government has requested SEBI to consider raising the minimum public shareholding in listed companies from the current threshold of 25% to 35%. This is a significant move as more domestic retail investors would be incentivised to participate in listed stocks.

Following measures have been proposed to ease FPI investment:

- Increasing the statutory limit for FPI investment in a company from 24% to the respective sectoral cap with option given to the concerned corporates to limit it to a lower threshold; this was the other way round earlier, where companies were required to pass a special resolution to enhance the limit from 24% to the sectoral cap.

- Permitting subscription to listed debt securities issued by Real State Infrastructure Trusts and Investment Infrastructure Trusts;

- Allowing investments made by FIIs/FPIs in debt securities issued by infrastructure debt funds - non-banking financial companies (IDF-NBFCs) to be transferred and sold to any domestic investor within the specified lock-in period; and

- Rationalization and streamlining of existing KYC norms for FPIs making it more investor-friendly without compromising the integrity of cross-border capital flows.

The Proposal for Public Sector Banks to be capitalised by an amount of Rs.70,000 crores should give a boost to credit flow into the economy. This should also finance the purchase of high-rated pooled assets of financially sound Non-Banking Financial Companies(NBFC), amounting to a total of Rupees one lakh crore during the current financial year. The above proposal in addition to the government providing a one-time six-month partial credit guarantee to the Public Sector Banks for their first loss of up to 10% against the purchase of these pooled assets should go a long way in improving the distress the NBFC sector is facing.

The regulatory authority over housing finance sector is proposed to be returned from National Housing Board (NBFC) to the Reserve Bank of India (RBI). Also, Government has announced its intention to invest 100 lakh crore in infrastructure over the next five years.

Government has set an ambitious target of Rs. 1,05,000 crore of disinvestment receipts for the financial year 2019-20. The Government will undertake strategic sale of Public Sector Undertakings (PSUs) including the Air India. The Government will also continue to do consolidation of PSUs in the non-financial space as well.

A significant announcement is that the Government will start raising a part of its gross borrowing programme in external markets in external currencies. Further, it is proposed to raise sovereign debt from overseas markets. Given that India's sovereign external debt to GDP is among the lowest globally at less than 5%, the above step is a good way to reduce fiscal deficit while keeping the developmental needs of the country on track. It is expected that the Indian railways and power finance corporations could be the biggest beneficiaries of these steps.

Infrastructure Development:

The Government will carry out a comprehensive restructuring of National Highway Programme to ensure that a National Highway Grid of desirable length and capacity is created using a financeable model. After completing the Phase 1 of the Bharatmala, in the second Phase, States will be helped to develop State road networks.

India is now world's third largest domestic aviation market and the government feels the need to promote a robust aircraft financing and leasing activities within the country. To this effect, the International Financial Services Centre (IFSC) has been suggested as a good location to house such financing and leasing activities. It has been proposed to leverage India's engineering advantage and potential to achieve self-reliance in the vital aviation segment of Maintenance, Repair and Overhaul (MRO).

New Space India Limited (NSIL) has been incorporated as a new commercial arm of Department of Space to tap the benefits of the Research & Development carried out by ISRO.

An estimated investment of INR 50 lakh crores between 2018-2030 has been envisaged in Railway Infrastructure. This investment will be planned through the Public-Private Partnership mode to unleash faster development and completion of tracks, rolling stock manufacturing and delivery of passenger freight services.

Government plans to work towards connectivity infrastructure through "One Nation-One Grid" model. It has been proposed to create a blueprint this year for developing gas grids, water grids, i-ways and regional airports.

It is proposed that several reform measures would be taken up to promote rental housing. A Model Tenancy Law, considering the fact that the existing law is archaic, will also be finalized and circulated to the States for them to adopt.

To boost infrastructure financing, following measures are being suggested:

- Credit Guarantee Enhancement Corporation to be set up in 2019-20
- Action plan to deepen long term bonds market

Second phase of FAME (Faster Adoption and Manufacture of hybrid & Electric Vehicles in India) Scheme, with an outlay of INR 10,000 crore for a period of 3 years has been proposed to encourage faster adoption of Electric vehicles by way of offering upfront incentive to customers on purchase of Electric vehicles and for using these funds for establishing the necessary charging infrastructure for electric vehicles (advanced battery and registered e-vehicles). It is also proposed to provide tax benefits for Electric Vehicle by reducing the GST rate to 5% and tax incentive on purchase of Electric Vehicle.An additional income tax deduction of INR 1.5 lakh on the interest paid on loans taken to purchase electronic vehicle is also proposed under Income tax law.

To boost the economic growth and Make in India, the government has announced the launch of a scheme to invite global companies through a transparent competitive bidding to set up mega-manufacturing plants in sunrise and advanced technology areas such as Semi-conductor Fabrication (FAB), Solar Photo Voltaic cells, Lithium storage batteries, Solar electric charging infrastructure, Computer Servers, Laptops, etc. and provide them investment linked income tax exemptions under section 35 AD of the Income Tax Act, and other indirect tax benefits. However, there is no corresponding amendment to the Income Tax Act that is proposed this year.

Rural India and Farmers Welfare:

It has been proposed to upgrade roads connecting villages to rural markets. The Pradhan Mantri Grameen Sadak Yojana-III (PMGSY-III) has envisaged the upgradation of 1,25,000 kms of road length over the next five years, with an estimated cost of Rs. 80,250 crores. Government will also set up 80 Livelihood Business Incubators (LBIs) and 20 Technology Business Incubators (TBIs) in 2019-20 to develop 75,000 skilled entrepreneurs in agro-rural industry sectors. There is also a plan to set up 10,000 new Farmer Producer Organizations, to ensure economies of scale for farmers over the next five years. Further, Government proposes to expand the Swachh Bharat Mission to undertake sustainable solid waste management in every village.

Government has proposed that it will ensure drinking water to all rural households by 2024 under Jal Jeevan Mission. Focus on Integrated demand and supply side management at local level, creation of local infrastructure for rainwater harvesting, groundwater recharge and household waste water management.

Youth, Education, Women and MSME's:

Government propose to establish a National Research Foundation (NRF) to fund, coordinate and promote research in the country.

An amount of INR 400 crore has been provided under the head, "World Class Institutions", for FY 2019-20, more than three times the revised estimates for the previous year. India has the potential to become a hub of higher education and therefore, Government proposes to start a programme, 'Study in India', that will focus on bringing foreign students to study in Indian higher educational institutions. Further, a National Sports Education Board for Development of Sportspersons would be set up under Khelo India Scheme.

Government propose to streamline multiple labour laws into a set of four labour codes. This will ensure that process of registration and filing of returns will get standardized and streamlined. Further, Start Up India Scheme shall be continued for the entire period coinciding with the 15th Finance Commission period of 2020-25.

The Pradhan Mantri Shram Yogi Maandhan has been extended to provide Rs. 3,000 per month as pension on attaining the age of 60 to all workers in unorganized and informal sectors.

For every verified women Self Help Group (SHG) member having a Jan Dhan Bank Account, an overdraft of Rs. 5,000 is to be permitted. One woman in every SHG will also be made eligible for a loan up to Rs. 1 lakh under the MUDRA Scheme.

Under the Interest Subvention Scheme for Medium & Small Manufacturing Enterprises (MSMEs), INR 350 crores has been allocated for FY 2019-20 for 2% interest subvention for all GST registered MSMEs, on fresh or incremental loans. An online portal has been introduced providing of loans up to 1 crore for MSMEs within 59 minutes.

Direct Tax:

Personal Tax:

For ease of tax payments, Aadhar and PAN card are being made interchangeable. Tax Payers without PAN can file their return of income by quoting Aadhar number.

Increase in surcharge for "super-rich":

Budget 2019 proposed to increase the surcharge from 15 per cent to 25 per cent on taxable income between Rs. 2-5 crore and from 15 per cent to 37 per cent for income above Rs 5 crore. The effective tax rates for these two slabs is now 39% and 42.75% respectively. This has been a significant dampener to HNI's and has also raised concerns around taxation of income of certain pass through investment funds.

Change in Corporate Tax Rate:

Gradual reduction of domestic tax rate, along with withdrawal of various special tax benefits has been the stated aim of the current Government. In line with the same, the budget proposes to extend the beneficial tax rate of 25% to companies with turnover more than INR 400 Crores, up from INR 250 Crores.

While the increase in turnover seems substantial, the beneficial rate has been estimated to affect approximately about 4000 companies, which were there in the Rs. 250-400 Crore turnover segment.

Widening of Tax Base:

A proposal has been made to bring a large number of tax payers into the ambit of filing the income tax return by making it mandatory for filing of return of income in cases of:

- deposits in current account exceeding Rs 1 crore annually, or
- expenditure incurred for foreign travel exceeding Rs 2 lakh for self or any other person, or
- electricity expenditure exceeding Rs 1 lakh in a year, or
- fulfilment of other prescribed conditions

Further, Individuals and HUFs (not subject to tax audit) are currently not liable to withhold tax on payments made for contractual and professional services. Such payments will now be subject to withholding tax at the rate of 5% where such payments exceed Rs 50 lakh in a financial year.

Buy-back tax on listed companies:

Currently, unlisted companies are required to pay tax at the rate of 20% on buy-back of shares. This provision has been extended to buy-back by listed companies on or after 5 July 2019. Post this amendment, buy-back is taxable in the hands of the company and exempt in the hands of the shareholders. The rationale behind introduction of this section is the practice by various listed companies of using the buy-back route, as a way of distributing profits, instead of paying dividends, thereby saving on the lower tax rates applicable to buy-back vis-à-vis dividends.

Tax on gift to a non-resident:

The scope of "income deemed to accrue or arise" has been widened to include gift of money or property situated in India by a resident to a non-resident. Gifts to relatives or on the occasion of marriage etc., shall continue to be exempt from this provision. A non-resident may claim relief under the relevant tax treaty but it may not be possible in several jurisdictions; however, tax credit would be available in those cases.

National Pension Scheme (NPS):

Exemption limit on the commuted amount of the NPS scheme has been increased from 40% to 60% of the total NPS accumulation.

Affordable Housing:

Housing has been an area of concern for middle and lower-middle class. Further, real estate sector plays a significant role in generating employment in the economy. In order to incentivise purchase of affordable houses, it is proposed to provide an additional deduction upto Rs. 1,50,000 for interest paid on loan taken for purchase of residential house having value upto Rs. 45 lakh. This shall be in addition to the existing interest deduction of Rs. 2 lakh. Further, an alignment has been made of the definition of affordable housing with GST Acts.

The aforesaid loan is applicable on loans sanctioned in the FY 2019-2020. Considering the fact that only few months remain till March 2020, the Finance Bill has used the word "sanctioned", thereby covering loans sanctioned till 31 March, but where disbursement occurs Post the year end. This move may not be a significant incentive for affordable home buyers as the interest cost for such homes does not usually exceed Rs 2 Lakh per year anyway.

Digital Payment and faceless e-assessment:

Moving ahead on digitisation of compliances and assessments, the Finance Minister announced that assessments shall be carried out electronically by randomly allocated officers, thereby minimising human intervention. However, there is no clear road map described on the implementation of this proposal.

Further, with the objective of ensuring accuracy of reporting of income and taxes, pre-filled tax return forms based on data captured from stock exchange, banks, mutual funds, etc. will be provided to taxpayers. While the pre-filled returns are a good initiative, it would be preferable to ensure that the pre-filled details can also be modified, to ensure that the taxpayer has the option to modify any incorrect information.

Promoting cashless economy:

With a view to promote digital payments and cashless economy, following changes have been proposed:

- A proposal of tax withholding of 2% on cash withdrawals of more than INR 1 crore in a year from bank account has been made. Some business models, where large cash withdrawal is a necessity are proposed to be exempted.

  In this regard, it is important to note that the section uses the word "an Account". Clarification in this regard is required from the Government regarding whether the withholding tax needs to be undertaken on a per Account or Per Bank or Per Person basis.

- Permitted non-cash modes of payments have been widened to include all electronic modes as may be notified. This was earlier restricted to electronic clearing system and account payee cheque/draft.

- Businesses with turnover exceeding INR 50 crore are required to provide the facility to customers of making payment through prescribed electronic modes from 1 November 2019.

  The acceptable modes have not yet been prescribed, however the same is expected to include UPI, Digital wallets etc.

Start Ups:

The budget gave the Start-ups a lot of reasons to be happy. A major investment enabler in favour of start-ups was the existence of Section 54GB, which had a sun-set date of 31 March 2019, thereby threatening the incentives available for investments into start-ups. Section 54GB provides capital gains exemptions where the proceeds are invested in start-ups subject to various conditions. Two of the said conditions require the investor to hold at least 50% in the start-up and the start-up to hold all assets, which *inter alia* including computer and computer software, for a period of at least 5 years.

The budget has proposed to extend the sun-set date by 2 years to 31 March 2021, relaxing the shareholding condition to 25% and relaxing the period of holding conditions for computer and computer software to 3 years.

Further, the Start-ups would be eligible to carry forward loss provided either of the following conditions is satisfied:

- All the shareholders with voting rights continue to hold those shares, or
- At least 51% of the voting rights are held by the same shareholders.

International Financial Service Centre:

Budget 2019 laid down emphasis on promotion of International Finance Service Centre to make the GIFT city more competitive and attractive for global investors. In addition to the already existing tax incentives a series of tax relief measures have been proposed which are as follows:

- The tax holiday for the units in IFSC has been increased to 100% for 10 consecutive years out of a block of 15 years. Currently, it is 100% for the first five years and 50% for the balance five years.
- Transfer of derivative instruments or specified securities by a Category III Alternative Investment Funds (AIF) on a recognised stock exchange in an IFSC will be exempted from capital gains tax.

- Interest earned by non-resident lenders on loans to units in IFSC will be exempted from tax.

- Dividend declared by units in IFSC on or after 1 September 2019 from profits accumulated post 1 April 2017 will be exempted from dividend distribution tax.

  Income distributed on or after 1 September 2019 by mutual funds located in IFSC to non-resident unit holders will be exempted from additional tax on distribution.

It is important to note that this is the only exception to the stated purpose of the government to do away with tax holidays and similar benefits.

It is proposed to reduce Net Owned Fund requirement from INR 5,000 crore to INR 1,000 crore for NBFCs to facilitate on-shoring of international insurance transactions and to enable opening of branches by foreign reinsurers in the International Financial Services Centre.

Incentives to Non-Banking Financial Companies:

Interest on non-performing assets (NPAs) is taxed on receipt basis in case of banks. This benefit is now being extended to non-banking financial companies (NBFCs). Consequently, deduction of interest cost shall be permitted to the borrower only in the year of payment.

Measures for resolution of distressed companies:

Currently, tax losses are allowed to be carried forward for companies when there is a change in shareholding pursuant to a resolution plan approved under the Insolvency and Bankruptcy Code ("IBC").This benefit is now extended to companies (including their subsidiaries/step-down subsidiaries) where the change in shareholding and management is consequent upon a resolution plan approved by the National Company Law Tribunal ("NCLT") in cases of oppression and mismanagement.

For the purpose of computing Minimum Alternate Tax ("MAT") for such companies, the aggregate of book loss and unabsorbed depreciation shall be deductible.

Exemption from tax on issue of shares:

Investments made by Category I Alternate Investment Fund ("AIF") are currently exempt from taxation on notional income arising on issue of shares. This exemption is now extended to investment received from Category II AIF.

Non-business losses of investment fund available to unitholders

Category I and II AIFs are taxed only in respect of business income. Non-business income is taxed in the hands of the unitholders while the AIFs are treated as pass-through entities. It is now clarified that non-business losses shall also be allowed to be set off against income by the unitholders, subject to the satisfaction of the holding period conditions.

Indirect Taxes:

To simplify the GST process, a simplified monthly return has been introduced. Further taxpayers having annual turnover of Rs 5 crores are now required to file only quarterly returns. In order to make things easier and transparent, it is proposed to move to an electronic invoicing system wherein invoice details will be captured in a central system at the time of issuance. This will eventually be used to prefill the taxpayer's returns. Electronic invoice system will significantly reduce the compliance burden.

Exemption from Basic Custom Duty is proposed for import of defence equipment. Exemption to be withdrawn on certain electronic item which are being manufactured in India. Custom duty @5% to be levied on imported books to encourage domestic publishing and printing industry.

With a view to promote domestic manufacturing, custom duty reductions are proposed on certain raw materials and capital goods such as inputs for manufacture of artificial kidney and disposable sterilised dialyser, and fuels for nuclear power plants. To further incentivise e-mobility, customs duty is being exempted on certain parts of electric vehicles and capital goods required for manufacture of specified electronic goods. Custom duty on gold and other precious metals is proposed to increase from 10% to 12.5%. Also, a nominal basic custom duty is being proposed on tobacco products and crude.

Considering all the pending service tax litigation (pre GST regime), Government proposes a Legacy Dispute Resolution Scheme that will allow quick closure of these litigations. The proposed Scheme covers past disputes of taxes which have got subsumed into GST and also provides for method of payment of tax dues, arrears and restrictions regarding the manner of payment etc.

Budget 2019 Few prominent misses:

While the budget gave a lot of benefits to various sectors, there were also few misses. Most importantly, the expectation of extension of sunset clause of the Special Economic Zone tax benefits was not fulfilled. The middle-class taxpayers also did not receive any relief in the form of additional deductions or improved slab rates.

Budget 2019 remained silent on the introduction of the Direct Tax Code although there was a general expectation that there would be certain mentions about it. The wait would hopefully end when the report is made available, by end July 2019. Further, the corporate tax rate reduction by increasing the threshold has benefitted very few companies, it should be noted that the reduced corporate tax rate of 25% was promised to all the Indian companies without any threshold criteria.

One sector which did not get the desired attention from a Foreign Direct Investment perspective was the Defence Sector where there was expectation that the government route for FDI in the Sector would be increased from 49% to 74%. This move was required considering the immediate need for transfer of technology and know-how required for the rapid growth and development of the defence equipment manufacturing sector. Further, steep increase.

Though may not be intended but steep increase on super rich may also adversely affect the foreign investment inflows in India as few of the FPIs and AIFs which are structured as trust and considered as opaque may have to shell out significant additional tax till they are re-structured efficiently.

Conclusion:

Overall Budget 2019 is a balanced approach by new government providing impetus to the industrial growth, where there were feeling that industrial sector was almost overlooked in the interim budget presented in February 2019. Though there are a lot of proposals in the budget 2019, it shall be interesting to see the fine print when such proposals are put into place, if the proposals are implemented in right earnest Indian Economy certainly on course of USD 5 trillion economy by 2024.

INDO-JAPAN CHAMBER OF COMMERCE & INDUSTRY
No. 21, Kavignar Bharathidasan Road, Teynampet, Chennai 600 018.
Tel: 91-44-2435 2010 / 2435 4779 / 4855 6140 E-mail: indo-japan@ijcci.com Website: www.ijcci.com