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From Editorial Desk

Dear Readers,

Welcome to the March Edition of FINSCAPE.

This edition of FINSCAPE focuses on the budget presented by the Finance Minister. Affirming that the economy is right on track, Finance Minister Arun Jaitley presented the Union Budget for 2016-17.

Financial sector set for overhaul under the budget proposals. Govt. vows to push crucial bankruptcy code, pass amendments to RBI, SEBI Acts; will let sponsors of ARCs hold up to 100% stake

The two other key points of impact on banking and insurance are i. Banks get a big boost: Rs 25,000 crore towards recapitalisation of public sector banks and ii. General Insurance companies will be listed in the stock exchange

Happy reading.

Regards,

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Co-ordinator- CFS

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Head lines:

HIGHLIGHTS OF UNION BUDGET 2016-17

- Affirming that the economy is right on track, Finance Minister Arun Jaitley presented the Union Budget for 2016-17. Citing that the CPI inflation has come down to 5.4% from 9 plus, he said it is huge relief for the public.
- Following are the proposals under various categories:

TAX

- Infrastructure and agriculture cess to be levied.
- Excise duty raised from 10 to 15 per cent on tobacco products other than beedis
- 1 per cent service charge on purchase of luxury cars over Rs. 10 lakh and in-cash purchase of goods and services over Rs. 2 lakh.
- SUVs, Luxury cars to be more expensive. 4% high capacity tax for SUVs.
- Companies with revenue less than Rs 5 crore to be taxed at 29% plus surcharge
- Limited tax compliance window from Jun 1 - Sep 30 for declaring undisclosed income at 45% incl. surcharge and penalties
- Excise 1 per cent imposed on articles of jewellery, excluding silver.
- 0.5 per cent Krishi Kalyan Cess to be levied on all services.
- Pollution cess of 1 per cent on small petrol, LPG and CNG cars; 2.5 per cent on diesel cars of certain specifications; 4 per cent on higher-end models.
- Dividend in excess of Rs. 10 lakh per annum to be taxed at additional 10 per cent.

Personal Finance

- No changes have been made to existing income tax slabs
- Rs 1,000 crore allocated for new EPF (Employees' Provident Fund) scheme
- Govt. will pay EPF contribution of 8.33% for all new employees for first three years
- Deduction for rent paid will be raised from Rs 20,000 to Rs 60,000 to benefit those living in rented houses.
- Additional exemption of Rs. 50,000 for housing loans up to Rs. 35 lakh, provided cost of house is not above Rs. 50 lakh.
- Service tax exempted for housing construction of houses less than 60 sq. m
- 15 per cent surcharge on income above Rs. 1 crore

Social

- Rs. 38,500 crore for Mahtma Gandhi MGNREGA for 2016-17
- Swacch Bharat Abhiyan allocated Rs.9,500 crores.
- Hub to support SC/ST entrpreneurs
- Government is launching a new initiative to provide cooking gas to BPL families with state support.
- LPG connections to be provided under the name of women members of family: Rs 2000 crore allocated for 5 years for BPL families.
- 2.87 lakh crore grants to gram panchayats and municipalities - a quantum jump of 228%.
- 300 urban clusters to be set up under Shyama Prasad Mukherji Rurban Mission
- Four schemes for animal welfare.

Health

- 2.2 lakh renal patients added every year in India. Basic dialysis equipment gets some relief.
- A new health protection scheme for health cover upto 1 lakh per family.
- National Dialysis Service Prog with funds thru PPP mode to provide dialysis at all district hospitals.
- Senior citizens will get additional healthcare cover of Rs 30,000 under the new scheme
- PM Jan Aushadhi Yojana to be strengthened, 300 generic drug store to be opened

Education

- Scheme to get Rs.500 cr for promoting entrepreneurship among SC/ST
- 10 public and 10 private educational institutions to be made world-class.
- Digital repository for all school leaving certificates and diplomas. Rs. 1,000 crore for higher education financing.
- Rs. 1,700 crore for 1500 multi-skill development centres.
- 62 new navodaya vidyalayas to provide quality education
- Digital literacy scheme to be launched to cover 6 crore additional rural households
- Entrepreneurship training to be provided across schools, colleges and massive online courses.
- Objective to skill 1 crore youth in the next 3 years under the PM Kaushal Vikas Yojna-FM Jaitley
- National Skill Development Mission has imparted training to 76 lakh youth. 1500 Multi-skill training institutes to be set up.

Energy

- Rs. 3000 crore earmarked for nuclear power generation
- Govt drawing comprehensive plan to be implemented in next 15-20 years for exploiting nuclear energy
- Govt to provide incentive for deepwater gas exploration
- Deepwater gas new disc to get calibrated market freedom, pre-determined ceiling price based on landed price of alternate fuels.

Investments and infrastructure

- Rs. 27,000 crore to be spent on roadways
- 65 eligible habitats to be connected via 2.23 lakh kms of road. Current construction pace is 100 kms/day
- Shops to be given option to remain open all seven days in a week across markets.
- Rs. 55,000 crore for roads and highways. Total allocation for road construction, including PMGSY, - Rs 97,000 crore
- India's highest-ever production of motor vehicles was recorded in 2015
- Total outlay for infrastructure in Budget 2016 now stands at Rs. 2,21,246 crore
- New greenfield ports to be developed on east and west coasts
- Revival of underserved airports. Centre to Partner with States to revive small airports for regional connectivity
- 100 per cent FDI in marketing of food products produced and marketed in India
- Dept. of Disinvestment to be renamed as Dept. of Investment and Public Asset Management
- Govt will amend Motor Vehicle Act in passenger vehicle segment to allow innovation.
- MAT will be applicable for startups that qualify for 100 per cent tax exemption
- Direct tax proposals result in revenue loss of Rs.1060 crore, indirect tax proposals result in gain of Rs.20,670 crore

Agriculture

- Total allocation for agriculture and farmer welfare at Rs 35984 crores
- 28.5 lakh heactares of land wil be brought under irrigation.
- 5 lakh acres to be brought under organic farming over a three year period
- Rs 60,000 crore for recharging of ground water recharging as there is urgent need to focus on drought hit areas cluster development for water conservation.
- Dedicated irrigation fund in NABARD of Rs.20.000 cr
- Nominal premium and highest ever compensation in case of crop loss under the PM Fasal Bima Yojna.

Banking

- Banks get a big boost: Rs 25,000 crore towards recapitalisation of public sector banks. Jaitley says: Banking Board Bureau will be operationalised, we stand solidly behind public sector banks.
- Target of disbursement under MUDRA increased to 1,80,000 crore
- Process of transfer of government stake in IDBI Bank below 50% started
- General Insurance companies will be listed in the stock exchange
- Govt to increase ATMs, micro-ATMs in post offices in next three years

Other proposals in Budget 2016 impacting Financial Services Sector

Securitisation trusts

Currently, the special taxation regime is provided in respect of income of securitisation trusts and the investors of such trusts. The regime provides that the income distributed by such a trust to its investors shall be subject to a distribution tax and such income shall be exempt in the hands of the investors. Investors such as banks suffered a disallowance of expenditure in respect of such exempt income.

The Finance Bill proposes a new regime under which there shall not be any distribution tax on such income. However, there shall be a withholding tax on distribution of income by the trust. Further, the provisions are now extended even to trusts set up by a securitisation company or a reconstruction company. These changes shall go a long way in developing the market for such trusts in India.

Deduction for the non-performing assets (NPA) provision to NBFCs

The financial services industry, especially the banking/NBFC sector, is undergoing turmoil in light of the alarming level of NPAs. Currently, banks, public and state financial institutions are allowed deduction in respect of provision for NPAs up to a prescribed limit. NBFCs, which have been a significant source of lending to crucial sectors such as infrastructure and housing, were not permitted to claim such a deduction for provision on NPAs. The Finance Bill proposes to grant such deduction even to NBFCs up to 5 per cent of the total income.

Onshore fund management industry

The Budget 2015 introduced special regime for offshore investment funds to boost the domestic fund management industry. These provisions have been rationalised to provide that eligible investment fund would also include a fund established outside India in a notified country. This will help in including pension funds, mutual funds, SICAVs, etc that were earlier not covered as it was ambiguous if they qualify as tax resident of such countries due to domestic law framework.

Alternative investment funds (AIFs)

Currently, the income earned by investors from investments in Category I and II AIFs is subject to withholding tax rate of 10 per cent. Where the investor in such an AIF is a non-resident, there is a possibility that under the applicable tax treaty, the income is subject to tax at a lower rate/not subject to tax. Accordingly, the provisions have been rationalized to the effect that withholding tax as per tax treaty would apply to the income paid to a non-resident if it is more beneficial.

Business trust

Currently, in the case of business trusts being REITs and Infrastructure Investment Trust, the dividend distribution tax (DDT) is levied on the dividend distributed by the SPVs of the trusts. Under the present regulations, the business trusts have to distribute 90% of the income earned to its investors, which results in tax inefficiency. Accordingly, the provisions have been rationalised to the effect that the dividend distributed by the SPV would not be subject to DDT and the same would also be exempt in the hands of the trust and the investors.

Income Computation and Disclosure Standards (ICDS)

While, the Finance Minister emphasized the need to simplify existing income-tax law, the Bill does not defer the ICDS as suggested by various industry bodies and the Easvar Committee.

International Financial Services Centre (IFSC)

An IFSC is a jurisdiction that provides financial services primarily to non-residents in a foreign currency. It targets offshore business and deals only sparingly with residents. With an objective to incentivise the growth of IFSCs in India, the FB proposes to provide certain tax concessions to units in an IFSC. Minimum Alternative Tax (MAT) shall be levied at a concessional rate of 9 per cent on a unit in an IFSC against the normal MAT rate of 18.5%. Further, no tax will be levied on dividends distributed by a unit in an IFSC deriving income solely in foreign exchange. Further, no securities transaction tax and commodities transaction tax would be levied on transactions undertaken on an exchange located in the IFSC in foreign currency. However, no relief has been granted from withholding tax on payments made by a unit in an IFSC to non-residents.

MAT on foreign companies

Last year, the Finance Act, 2015 granted exemption to foreign companies from the ambit of MAT on a prospective basis. In line with the press release issued by the Government, the FB clarifies that MAT will not apply to foreign companies even for prior years in certain cases.

Taxation of income from offshore rupee-denominated bonds

Under the new external commercial borrowings framework, an Indian company is now permitted to issue rupee denominated bonds outside India. By a press release dated 29th October 2015, the Government announced that interest on such bonds will be taxable at a concessional rate of 5% and capital gains arising on their redemption would be exempt from tax. While the FB provides for exemption to capital gains earned on appreciation of rupee, the concessional rate of 5 per cent does not find a mention in the Budget proposals.

From the amendments proposed in the Budget, it is reassuring to note that the finance minister has taken cognizance of the various representation made by the stakeholders and accordingly amended the various provisions. This sends out a positive message to the taxpayers that the government is aware of the ground realities and looks forward to make the amendments that do not have tax revenue leakage and boost the industry confidence.

Insolvency code

The government on Monday said that it would bring in a new comprehensive Code on Resolution of Financial Firms during 2016-17, which will aim to resolve bankruptcy situations in banks, insurance companies and financial sector entities. “This Code, together with the Bankruptcy Code 2015, when enacted, will provide a comprehensive resolution mechanism for our economy,” Jaitley said in his budget speech.

The government introduced the Bankruptcy Code in the winter session of Parliament and through it aims to provide a one-stop solution for a firm to dissolve itself.

ARC reform

To improve the management of existing stressed assets, the government has proposed to allow sponsors of ARCs to hold up to 100% stake in companies and even allow non-institutional investors to invest in securitization receipts. This will require amendments to the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.

At present, sponsors of any ARC, typically banks or financial services companies, cannot hold more than 50% stake in the company. The remaining stake has to be held by individuals.

“If the amendment goes through, the ARCs can become majority-owned subsidiaries of their sponsor institution, which can make way for higher and cheaper capital, which is one of the biggest challenges in the sector right now,” said Eshwar Karra, chief executive officer (CEO) of Phoenix ARC Pvt. Ltd, in which Kotak Mahindra Bank Ltd owns a 49% stake.

Foreign holding in bourses

Another key change the government is targeting is allowing an individual foreign investor to hold up to 15% in an exchange, up from the current 5%, to increase global competitiveness of Indian stock exchanges.

The proposal was first mooted by Sebi in 2012, only to be turned down by the Bimal Jalan committee set up for amendments to stock exchanges and clearing corporations regulations.

In June 2014, Sebi once again proposed this to the government, arguing that the exchange space is now mature enough to handle higher participation from a single foreign investor, following which the ministry asked for feedback in November 2015. Mint reported on 26 February that the Sebi board on 12 March will take up the proposal to increase foreign shareholding in stock exchanges.

Other measures

Further, the government seeks to bring in a comprehensive legislation to tackle the menace of money pooling schemes and illegal deposit-taking. Currently, the numerous ponzi schemes end up falling under different regulators.

Finally, the budget listed six measures to deepen the corporate bond market that has emerged as a cheap source of borrowing as banks' loan rates remain high. One of them is to allow Life Insurance Corporation of India to set up a fund that will provide credit enhancements to bonds floated by infrastructure companies.

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