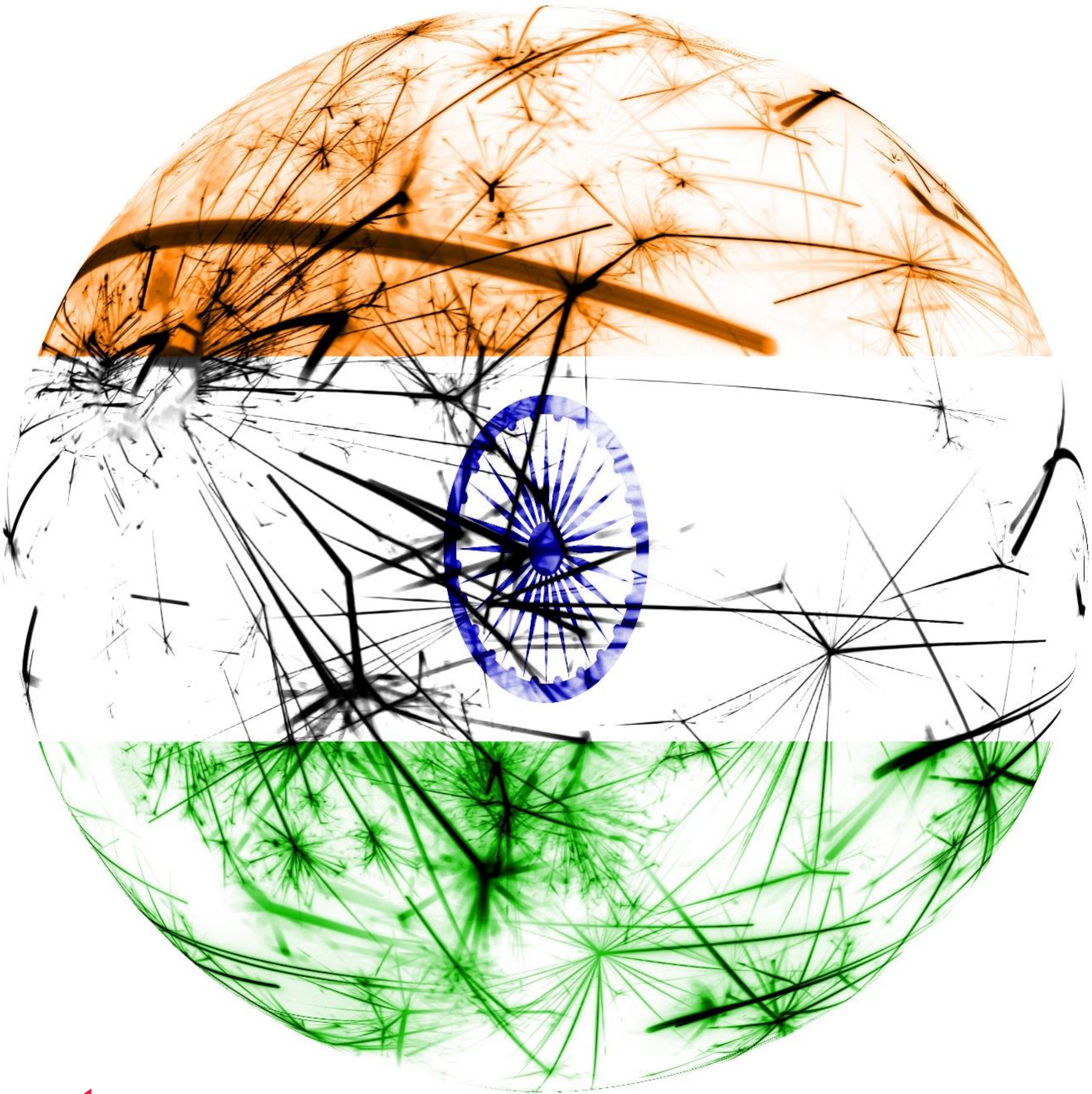
INDIA UNION BUDGET, 2019

KEY HIGHLIGHTS



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With a new electoral mandate, the Modi government 2.0 presented its first budget. The budget primarily focussed on infrastructure spending and boosting investments by private and foreign investors. The government forecasts that the Indian economy would grow to USD 05 trillion by 2025, which is almost twice its current size. With the budget announcements, a slew of reforms and policies are expected in the coming months for implementing these reforms, including the draft of the much-awaited Direct Tax Code, which aims to overhaul the present direct tax law.

We are highlighting some of the key amendments, relevant from a foreign investor's perspective.

1. Tax rates

The present base tax rate for Indian companies whose turnover did not exceed INR 2.5 billion is 25%, which is now extended to companies with a turnover of up to INR 4 billion. The proposal is thus likely to cover almost all Indian companies. Largely, tax rates have remained unchanged though there was contemplation of reducing the headline tax rate and extending to all business entities, including LLP.

2. Real estate

The government had earlier introduced a 'Housing for All' programme, which aimed to provide houses to eligible citizens by 2022. Over the next 3 years, the government proposes to provide 19.5 million houses under this programme. To boost its affordable housing programme, the budget proposes to relax the minimum square meter requirement per flat for the project to be classified as an affordable housing project, eligible to tax holidays.

3. Start-ups

To facilitate the startup culture in India, the budget proposes that start-ups and their investors who file requisite declarations and provide information in their returns will not be subjected to any kind of scrutiny in respect of funds raised by start-ups and valuations of share premiums. Also, special administrative arrangements will be undertaken for pending assessments of start-ups and redressal of their grievances. This provides a major relief to recognised start-ups who were penalised for being able to raise capital at premium rates.

At present, start-ups are not required to justify fair market value of their shares issued to certain investors, including Category-I Alternative Investment Funds (AIF). This benefit is now proposed to be extended to investment from Category-II AIF.

4. Electric vehicles manufacturing

The Government introduced an incentive scheme in 2015 to promote manufacturing of electric and hybrid vehicle technology and to ensure its sustainable growth. While the scheme has had limited success till now, the second phase of the scheme, having commenced from 01 April 2019, aims at providing upfront incentives on purchase of electric vehicles to encourage faster adoption. Towards this, the budget proposes to:

a) Slash the GST rate on electric vehicles from 12% to 5%

b) Provide an additional income tax deduction of INR 1.5 lakhs on interest paid on loans taken to purchase electric vehicles

c) Waiver-off customs duty on parts of electric vehicles such as e-drive assembly, on board charger, e-compressor and charging gun

The FM further mentioned that the government shall launch 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 etc. and offer them tax incentives.

All the efforts are being made to fulfil India's commitment to move to e-vehicles by 2030. These measures coupled with other associated activities such as, setting up charging stations for e-vehicles, creating necessary infrastructure like roads, highways etc, should give a major fillip to India's e-vehicle story.

5. Transfer Pricing adjustment

The concept of secondary adjustment was introduced in the Indian context in the year 2017. The erstwhile law provided that the Indian taxpayer was required to receive a sum representing the adjustment amount within the specified time limit, failing which a secondary adjustment would be made. The budget proposes to relax these provisions by:

a) Allowing receipt of such money from any other related party and not necessarily the party with whom there was an international transaction

b) Avoid repatriating the money to the Indian entity by making a payment of additional tax at an effective tax rate of 20.97%

Payment of additional tax should mitigate uncertainties prevailing around secondary adjustments.

6. Foreign Investments

- In order to boost foreign investments into India, the 24% ceiling of foreign portfolio investment shall be done away with and FPI investment shall be increased to sectoral limits. Non-Resident Investor ('NRI) portfolio investment route is proposed to be merged with FPI route. Overall, this should help bringing much larger pools of NRI capital through pooled and professionally managed structures
- The government shall decide for opening-up for FDI for sensitive sectors such as aviation, media and insurance.
- 100% foreign investment will be allowed for insurance intermediaries as against the current cap at 49%
- Local sourcing norms for FDI companies will be eased for single-brand retail sector; presently 30% is to be sourced locally

The relevant notification shall be issued in due course.

7. Incentives for units in International Financial Services Centre ('IFSC')

Budget of 2016 introduced a favourable tax regime for units operating in an IFSC. To boost investments into IFSCs, the budget proposes to provide tax incentives to units operating in IFSCs, viz:

a) Exempt Category III AIF, which has non-resident investors, from any capital gains derived from sale of specified securities (to be notified later), provided such income is in foreign exchange

b) Interest paid by a unit in IFSC to a non-resident in relation to a loan availed after 01 September 2019, shall be exempt from Indian taxes

c) Exemption from dividend distribution tax on any dividend distributed by units in IFSC, irrespective of whether they are from current profits or reserves

d) Tax holiday to units in IFSC extended to 100% for 10 consecutive years in a 15-year block

e) Minimum alternate tax applies to an IFSC unit at the rate of 9%

The GIFT city in Ahmedabad provides an early opportunity to financial services companies to setup base in a favoured tax and regulatory zone.

8. Increase of public shareholding in listed companies

The Hon'ble FM proposed that the minimum public shareholding in listed companies should be raised to 35% from the existing requirement of 25% after consultation with the Indian securities market regulator. While the move is aimed at enhancing liquidity in secondary markets and having a larger public say in listed companies, it remains to be seen how Indian listed companies, which are predominantly family driven, plan on meeting the requirements and at the same time ensuring that the stock price is not adversely affected. However, the dis-investment process is likely to present attractive investment opportunities to foreign investors wishing to invest in efficiently-managed family businesses.

9. Receipt of assets below fair value

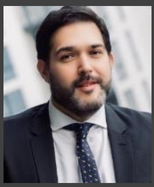
The domestic tax law provides that when any taxpayer, including a non-resident taxpayer, receives specified properties (eg.: shares) for a value which is below its fair market value, the recipient taxpayer would be subject to tax in India on the differential amount. The budget proposes to include the purported income arising in these situations within the scope of the deeming tax for a non-resident taxpayer; thereby enlarging India's taxing right, extra-territorially. One would however, be entitled to tax treaty protection, if any.

10. Social stock exchange

The Hon'ble FM proposed setting up of a Social Stock Exchange – an electronic fund-raising platform. The objective of this exchange would be to list social enterprises and voluntary organisations working for social welfare objective so that they can raise capital. As of now, India has been averse to foreign funds for not for profit activities and any such foreign investment has been highly regulated to ensure that foreign funds are not diverted for unwarranted purposes. While further details are awaited on the proposed platform, it remains to be seen whether the government would be open to attract foreign investors for companies to be listed on the social platform, in what appears to be a first by a government body across the globe.

The proposed changes to the policies and tax law indicates a direction which the government wishes to take with a hope of rejuvenated reforms. Once the proposed changes are implemented in the manner contemplated, the growth projected by the economic survey of 7% should be possible.

CONTACT US



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