Budget 2020-21 Readout

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TAXES

Direct Tax Proposals

Summary: Changes in direct taxes are unlikely to have a significant impact on revenue generation. However, a few positive changes, such as the abolition of Dividend Distribution Tax (DDT) for companies and income tax rationalization for individuals, may give a fillip to investments and consumption.

- Specific Measures
  - Dividend distribution Tax – With DDT scrapping for companies, dividends will be added to the recipients' taxable income bracket.
  - The Corporate Tax rate for existing companies slashed to 22% plus surcharge, including the resident cooperative societies if they do not claim any incentive/deductions. While the government has conferred a tax cut on corporates and manufacturing companies, the other forms of business enterprises still pay high tax at 30%.
  - Corporate tax rate of 15% is extended to the new power generation companies also in addition to the new manufacturing companies allowed since October 2019.
  - Proposal for 100% tax exemption on investment in infrastructure and other specified sectors subject to a lock-in period of 3 years.
  - A new simplified personal tax regime allows individuals to pay lower tax in case of no exemptions. This is a measure of boosting consumption by rationalizing the tax rates.
  - The rate for Tax deduction at source (TDS) in case of fees for technical services (other than professional services) is reduced to 2% from 10%.
  - 1% additional TDS on E-commerce players.

- International Tax & Transfer pricing
  - Budget 2020 proposes to defer the applicability of Simplified Employee Pension (SEP) to starting of Assessment year 2022-23. Certain drafting changes have also been made while deferring the proposal. For the purposes of determining SEP of a non-resident in India, the threshold for the aggregate amount of payments arising from the specified transactions and for the number of users were required to be prescribed in the Rules. However, since the discussion on this issue is still going on in G20-OECD BEPS project, these numbers have not been notified yet. G20-OECD report is expected by the end of December 2020.
  - Source-based taxation on income from
    - advertisements which targets customer residing in India/customers who access the advertisement through internet protocol address located in India.
    - sale of data collected from a person residing in India or from a person who uses internet protocol address located in India.
    - sale of goods or services using data collected from a person residing in India or from a person who uses internet protocol address located in India.

- Tax treaties will be aligned to the Multilateral Instrument so that they are not used for non-taxation or reduction of tax through evasion/avoidance.
  - Form 3CEB/transfer pricing report to be furnished by 31 October 2020.
  - Safe harbor provision and advance pricing agreement (including rollback) are amended to cover attribution of profits to a permanent establishment (PE).
  - Interest limitation rule is amended to exclude interest paid/payable on a loan extended by a PE of a non-resident bank for determining tax deductibility.

- Startups
  - Deferment of Employee Stock Ownership Plan (ESOP) taxation to 5 years or when the employee leaves job (whichever is earlier) subject to certain conditions.
  - For Income tax exemption under 80IAC, the turnover limit increased from INR 25 Crores to INR 100 Crores and duration from 7 years 10 years. 100% tax rebate on profits, for three out of a block of seven years, is available now to start-ups with an annual turnover of INR 25 crores (approximately $3.6 million). The tax benefits are now extended to start-ups with INR 100 crores (nearly $14 billion).
  - The turnover threshold for audit for start-ups and MSMEs has increased from INR 1 Crore to 5 Crores, leading to no audit for taxpayers carrying on business and having turnover up to INR 5 crores provided cash transaction is less than 5% in value.

- Litigation & compliance
  - Direct Tax dispute resolution scheme 'Vivaad se Vishwaas', waiving interest & penalty provided if the tax amount is paid by March 2020, will now close in June 2020.
  - The E-appeal process is introduced for ease of compliance, faceless, greater efficiency and transparency to the tax appeal is introduced.

- Compliance provisions
  - Instant allotment of PAN on the basis of Aadhaar.
  - The taxpayer charter, defining the taxpayer's rights clearly, to be institutionalized to curtail tax harassment and strengthen taxpayers-tax administration trust.
  - Business trusts are not required to be listed; this will allow them to pass-through under the Income Tax Law.
  - The return filing due date for corporates and taxpayers not liable to tax audit (non-TP cases) has been extended to 31 October although the due date for furnishing tax audit and other audit reports continues to be 30 September.
  - Issuance of Unique Registration Number to all charity institutions for easy tax compliance.

- Other important proposals
  - Carry forward of losses & depreciation is now allowed in case of amalgamations pertaining to amalgamated public sector banks and general Insurance companies.
  - Definition of 'Resident' for individuals amended for tax compliance purposes.

GST & Customs Proposals

Summary: The changes proposed in the GST are mostly positive, excluding the implementation timelines that seem difficult to achieve. However, an increase in cess (tax on tax) and excise duty are not conducive for the specific industry growth. The budget has proposed changes in basic customs duties to encourage domestic processing and manufacturing in the country. This involves raising customs duties and withdrawing exemption from some categories.

- Continued focus towards evolving the GST law and to resolve legislative and procedural issues across industry sectors.
- Digitization/e-invoicing under GST will be implemented in a phased manner starting 1 February 2020 on an optional basis to facilitate compliance and new return filing.
- Simplified GST returns and fully automated refund process will be implemented April 1, 2020.
- The imposition of 'Health Cess' on import of medical devices at the rate of 5% ad-valorem with immediate effect. However, the same shall not be imposed on parts/inputs or where Basic Custom Duty on said goods is exempt under any FTA notification.
- Basic customs duty on imports of newsprint and lightweight coated paper has been reduced from 10% to 5%.
- Rise in raise excise duty on Cigarettes and other tobacco products.
- The import tariff on whey powder, cheese, butter, ghee, butter oil has been increased from 30% to 40% to promote domestic production.
- Custom duty on isolated soy protein which was at 10% is increased to 30%.
- The basic customs duty on dietary soy fiber has been increased to 30% from the current 15%.
- Duty on Walnut (kernel) is raised from 30% to 100% to align with the duty on shelled walnuts.
- Review of Rules of Origin for sensitive items in order to arrest undue claims under FTA.
- Creation of an electronic duty credit ledger in the customs system to enable duty credit in lieu of duty remission to be given in respect of exports or other such benefits in electronic form for its users transfer and other activities. The credit can also be used to make payment of customs duties.

FISCAL MANAGEMENT

Summary: Fiscal management is going to be a huge challenge for the Government in the next financial year. The fiscal deficit target is contingent on almost 14% increase in direct taxes and INR 2.1 lakh crores ($30 billion approximately) worth of disinvestment proceeds – which seems a very ambitious target.

- Budget estimates a fiscal deficit of 3.8% in Revised Estimated 2019-20 and 3.5% for Budget Estimate 2020-21. These numbers indicate that the Government of India (GoI) has used the escape clause of the Fiscal Responsibility and Budget Management (FRBM) this year and the fiscal deficit is estimated to come down in the next fiscal based on the revenue receipts projection.

DISINVESTMENT

Summary: The disinvestment target ($30 billion – highest ever set by the GoI) is going to be a huge challenge for the Department of Investment and Public Assets Management (DIPAM). Public Sector Life Insurance Corporation IPO in this next fiscal seems a daunting task, given the complexity involved in the process. IDBI bank's stake sale may not fetch much of a non-tax revenue for the government.

- The GoI has proposed to sell Life Insurance Corporation (LIC) partially through Initial Public Offering (IPO). Budget documents have not specified the percentage of stake sale which is currently under consideration, but the Government is looking to mop up INR 90K Crores (more than $12 billion approximately) through the stake sale equivalent to 10% of LIC's paid-up capital.

- The budget proposed to sell the balance holding of Government of India in IDBI Bank to private, retail and institutional investors through the stock exchange. If implemented, the IDBI Bank may be fully owned by the private sector.

BANKING

Summary: Overall good measures in this sector. Long over-due Increase in deposit insurance coverage is a welcome move and is expected to encourage investments. Strengthening the supervisory framework for co-operative banks and sub-ordinate debt issuance for MSMEs is also a positive step.

- The budget proposed an increased in the public sector Deposit Insurance and Credit Guarantee Corporation (DICGC) deposit insurance coverage for bank deposits. The existing cover of INR 100K per depositor is increased to INR 500K per depositor. This announcement is aimed at mitigating the fear of bank depositors in the light of recent banking developments.
- Amendments to the Banking Regulation Act are aimed to strengthen co-operative banks in terms of professionalism, access to capital and improve governance and oversight mechanisms.
- To facilitate working capital requirements for the MSMEs, the budget proposed to allow banks to extend sub-ordinate debt to the MSME entrepreneurs.

NON-BANKING FINANCIAL COMPANIES (NBFCS)

Summary: While the proposed changes are welcome, more concrete measures were expected to help the troubled NBFC sector. Special measures were expected for the Housing Finance Companies (HFCs) which did not come through the budget.

- Currently, NBFCs with an asset size of INR 5 billion (more than $71 million) or more is allowed to exercise the right of recovery of dues under the SARFAESI Act, for a sum of INR 10 million (approximately $143K) and above. The budget proposed to reduce the thresholds and extend the relief to smaller NBFCs with an asset size of INR 1000 million (approx. $14 million) for a loan size of INR 5 million ($71K approximately) or more.
- NBFCs are allowed to extend invoice financing to MSMEs through the TReDS platform (an institutional mechanism set up to facilitate the trade receivable financing of MSMEs from corporate buyers). This is likely to help the MSMEs for their working capital requirements.
- The budget proposed to come up with a mechanism to further supplement liquidity support to NBFCs/HFCs. This is in addition to the Partial Credit Guarantee Scheme already announced earlier.
- The budget proposed to expand the National Bank for Ag & Rural Development's (NABARD's) re-financing scheme for NBFCs which are in the agricultural credit space.

CAPITAL MARKETS

Summary: Proposals for expanding the Govt Securities (G-Secs) market and the corporate bond market are welcome, but more measures were expected on the equity market side.

- The budget proposed that specific categories of G-Secs would be opened fully for non-resident investors. This is likely to increase the flow of capital into the country.

- The budget increased the limit for Foreign Portfolio Investments (FPIs) participation in Corporate Bonds from the existing 9% to 15% of the outstanding stock of corporate bonds. This will help increase the FPIs participation in the corporate bond market and in turn deepen the corporate bond market in India.
- The budget proposed to float a new debt-Exchange Traded Funds (ETFs) consisting mainly of G-Secs. This new product is likely to attract investments from retail investors, pension funds, and long-term investors, which may strengthen the G-Secs market.
- To expand the scope of Credit Default Swaps (CDS), the budget proposed a new law to lay down a mechanism for netting of financial contracts. The aim of the legislation is to strengthen the corporate bond market in India.
- The budget proposed to set-up an International Bullion Exchange in the International Financial Service Center-Gujarat International Finance Tec-City (IFSC-GIFT city) to bring trading volumes on-shore instead of off-shore.

SOVEREIGN WEALTH FUNDS (SWFS)

Summary: Tax exemption to SWFs would create a special avenue of long-term finance for the credit-starved infrastructure sector.

- Starting 1st April 2020, SWFs which satisfy prescribed conditions and are notified by the GoI shall be tax-exempt in India on any dividends, interests, and long-term capital gains realized from an investment made in India, whether in the form of debt or equity. This is subject to the following conditions:
    - It is made on or before 31st March 2024;
    - It is held for at least 3 years; and
    - It is in a company/enterprise carrying on the business of developing, or operating and maintaining, or developing, operating, and maintaining any infrastructure facility defined in Explanation to clause (i) of section 80-IA(4), or such other business as may be notified by the Central Government.

GOVERNANCE

Summary: All measures seem very positive, but the implementation of the measures is the key to the desired results. Fine prints of the changes will determine the effectiveness of these announcements.

- 'Taxpayer Charter' will be enshrined in the statutes.
- Companies Act will be amended to provide civil liability for many existing criminal liabilities. This is likely to boost the ease of doing business.
- Contract Act will be strengthened to enforce contracts more effectively.
- A new National Policy on Official Statistics is proposed which would use the latest technology including AI. This is aimed at improving the current statistical systems.

NEW ECONOMY

Summary: Most of the measures are welcome; however, it will require timely and full implementation. Data Centre park proposal seems to drive the broad data localization initiative which is currently underway.

- To bring out soon a policy to enable the private sector to build Data Centre parks throughout the country. It will enable firms to skillfully incorporate data at every step of their value chains.
- The budget provides INR 6000 crores ($857 million approximately) for Bharat Net Program in 2020-21. This is likely to connect a large number of people, especially from the rural areas, to connect to the internet.
- A digital platform would be promoted that would facilitate seamless application and capture of Intellectual Property Rights (IPRs). Also, in an Institute of Excellence, a Centre would be established that would work on the complexity and innovation in the field of IP.
- The budget provides an outlay of INR 8000 crore (more than $1 billion) over a period five years for the National Mission on Quantum Technologies and Applications. This likely gives a boost to advanced technology-related research.

INFRASTRUCTURE

Summary: National Logistics Policy will be a key policy initiative; however, details will be critical as India's infrastructure need a serious focus if India wants to achieve the desired level of growth. Other proposals are welcome with effective implementation.

- The budget proposes to monetize at least 12 lots of highway bundles of over 6000 km before 2024.
- The budget proposes to provide about INR 1.70 lakh cores (circa $24 billion) for transport infrastructure in 2020-21.
- The budget proposes to provide about Rs. 22000 crores (more than $3 billion) to power and renewable energy sector in 2020-21.
- The budget proposes to expand the national gas grid from the present 16200 km to 27000 km.

INDUSTRY, COMMERCE AND INVESTMENTS

Summary: The Incentive Scheme focused on manufacturing of mobile phones, electronic equipment etc. should be watched closely.

- The budget proposes to set up an 'Investment Clearance Cell', working through a portal, that will provide end to end facilitation and support, including pre-investment advisory, information related to land banks and facilitate clearances at the Centre and the State level.
- Proposal for a scheme focused on encouraging the manufacture of mobile phones, electronic equipment and semi-conductor packaging will be watched carefully as it will progress.
- After scrapping export subsidies provided until last year to the textiles industry, the formation of a National Technical Textiles Mission is proposed with a four-year implementation period from 2020-21 to 2023-24 at an estimated cost of INR 1480 crore (circa $210 million).

- To achieve higher export credit disbursement, a new scheme, NIRVIK is being launched, providing for higher insurance coverage, reduction in premium for small exporters and simplified procedure for claim settlements.
- The budget sets out INR 27300 crore (approximately $4 billion) for development and promotion of Industry and Commerce activities for the year 2020-21.

EDUCATION AND SKILLS

Summary: The Education sector is now open for foreign investments; albeit on certain conditions. Measures, when announced, will need careful examination. Also, sectoral allocations, compared with last year, are very low. More focus on skill development activities was expected.

- New Education Policy will be announced soon.
- Sourcing from External Commercial Borrowings and FDI will be enabled to facilitate the delivery of higher quality education.
- “Study in India” program, Ind-SAT, will be held in Asian and African countries for benchmarking foreign candidates who receive scholarships for studying in India for higher education.
- The government allocated INR 99300 crore ($14 billion) for the education sector and INR 3,000 crores (approximately $428 million) for skill development.

AGRICULTURE, IRRIGATION AND RURAL DEVELOPMENT

Summary: Credit target for the next year seems ambitious. The total allocations have only increased marginally vis-à-vis last year. Specific push to drive up the rural demand appears missing. The percentage increase in allocation is very low and in some sub-segments factually negative.

- Agriculture credit target for the year 2020-21 has been set at Rs. 15 lakh crores (approximately $21 billion). For the entire sector INR 2.83 lakh crores (circa $40 billion) has been allocated for the year 2020-21, with INR 1.60 lakh crores (about $23 billion) for Agriculture, Irrigation & allied activities and INR 1.23 lakh crores ($17 billion) for Rural Development & Panchayati Raj related activities.
- The budget provides for the health sector about INR 69000 crores (nearly $10 billion), subsuming INR 6400 crores (more than $910 million) set aside for Prime Minister Jan Arogya Yojana.
- Total allocation for Swachh Bharat Mission (Clean India) is about INR 12300 crores (approximately $1.76 billion) in 2020-21.
- The budget also proposed INR 3.60 lakh crores (more than $50 billion) for Jal (Water) Jeevan Mission.

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