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BUDGET 2016

Understanding the Business Impact

Impact on Financial Services

February 2016

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Regulatory

Foreign direct investment

- Foreign Direct Investment (FDI) in insurance sector (for insurance company, insurance brokers, third party administrators, surveyors and loss assessors, etc.) increased from 26% under automatic route (and up to 49% under approval route) and been proposed to increase to 49% under automatic route.
- FDI in asset reconstruction company registered with Reserve Bank of India (RBI) under Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 increased from 49% under automatic route (and up to 100% under approval route) and been proposed to increase to 100% under automatic route.
- Foreign Portfolio Investors (FPIs) will be allowed to hold up to 100% (existing 74%) of each tranche in securities receipts issued by Asset Reconstruction Companies (ARCs) subject to sectoral caps.
- Sponsors can hold up to 100% shareholding in ARC (existing 50%).

Investment through stock exchange

Investment limit for foreign entities in Indian stock exchanges will be enhanced from 5% to 15% on par with domestic institutions.

FPI investment in Central Public Sector Enterprises (other than banks)

Existing limit of FPI investment of 24% to be raised to 49% subject to prior approval of Central Government in Central Public Sector Enterprises (other than banks).

Non-Banking Financial Companies (NBFC)

FDI will be allowed beyond existing 18 specified NBFC activities in the automatic route in other activities which are regulated by financial sector regulators.

FDI instruments

Hybrid instruments to be permitted subject to certain conditions.

Other regulatory reforms

- 1.Companies Act, 2013 to be amended for ease of doing business including improving the enabling environment for start-ups.
- 2.RBI Act 1934 to be amended to provide statutory basis for a Monetary Policy Framework and constitution of Monetary Policy Committee.
- 3.A comprehensive Code on Resolution of Financial Firms will be introduced.
- 4.A roadmap for consolidation of Public Sector Banks is to be provided.

Direct Tax proposals

- Corporate tax rate is proposed to be reduced to 29% in case of domestic companies having a total turnover or gross receipts up to 5 crores. In other cases, the corporate tax rate remains unchanged.
- Rate of Securities Transaction Tax (STT) on sale of option in securities where such option is not exercised is proposed to be increased from 0.017% to 0.05% of the option premium.
- Income by way of dividend in excess of INR 1 million shall be chargeable to tax in the case of individuals, HUF or a firm who is a resident of India at the rate of 10%. The taxation of dividend income in excess of INR 1 million shall be on a gross basis.
- 100% deduction of profits proposed to be granted for developing and building affordable housing projects approved before 31 March 2019, subject to conditions.
- As regards Gold Monetisation Scheme, 2015, the deposit certificates are proposed to be excluded from the capital gains taxation and the interest thereon is also proposed to be exempted from tax.
- Capital gains arising to a non-resident on appreciation of Rupee in case of Rupee denominated bonds is proposed to be exempt from tax.
- Transfer of a unit held in the consolidating plan of a mutual fund scheme made in consideration of allotment of units in the merged scheme is proposed to be exempt from capital gains tax.
- Exemption from levy of Dividend Distribution Tax (DDT) on dividend paid by an Indian company to a Business Trust (Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InvITs) with certain conditionality attached. The dividend is also proposed to be tax exempt in the hands of recipient i.e. Business Trust and its investors.
- Conditions of special taxation regime for offshore funds modified to include funds established/ incorporated outside in a country or territory notified by Central Government. Additionally, condition of fund not controlling and managing any business in India or from India shall be restricted only in the context of activities in India.
- Benefit of deduction of provision for bad and doubtful debts up to 5% of total income is proposed to be extended to NBFC.
- Following the recommendation of Committee headed by Justice A.P. Shah, it is proposed to clarify that provisions of Minimum Alternate Tax (MAT) does not apply to foreign companies not having permanent establishment in India.
- It is proposed to clarify that long term capital gain arising on transfer of shares of company in which public are not substantially interested will be taxable at 10%.
- In the Finance Minister's speech, period for getting benefit of long-term capital gain regime in case of unlisted companies is proposed to be reduced from 3 years to 2 years. However corresponding provision not reflected in Finance Bill, 2016.
- As per the proposed amendment, Category – I and Category – II Alternative Investment Fund (AIF) may consider Double Taxation Avoidance Agreement (DTAA) rates while making payments to its non-resident investors.
- New regime proposed to be introduced from securitization trust and its investors, and to provide tax pass through treatment.

International Financial Services Centre (IFSC)

- No STT where consideration is paid or payable in foreign currency.
- Long Term Capital Gains (LTCG) from transaction in foreign currency exempt even if STT not paid.
- Dividend declared by a unit located in IFSC and deriving income solely in convertible foreign exchange, will not be subject to DDT if the dividend is declared out of its current income.
- Book profit of a company being a unit located in IFSC, deriving income solely in convertible foreign exchange will be subject to MAT at 9%.

General

- Higher Tax Deduction at Source (TDS) @ 20% not to be charged on payments made to non-residents, on submission of alternate documents to Permanent Account Number (PAN) card.
- General Anti Avoidance Arrangement (GAAR) likely to come into effect from 1 April 2017.
- Limited tax compliance window from Jun 1 - Sep 30 for declaring undisclosed income at 45% including 7.5% surcharge and 7.5% penalties. 7.5% surcharge on undisclosed income (to be known as Krishi Kalyan surcharge) to be used for agricultural sector.
- In line with the Base Erosion and Profit Shifting (BEPS) Action Plan 1, it is proposed to charge an equalisation levy of 6% on the amount of consideration paid to a non-resident service provider by a resident in connection with specified services such as online/ digital advertisement. Obligation to deduct and deposit the equalization levy is on the payer.
- Distribution tax under buyback is proposed to be extend to all types of buyback under Companies Act, 1956 and Companies Act, 2013.
- Country-By-Country reporting requirements proposed to be introduced in line with BEPS Action Plan 13.
- Conditions for tax neutral conversion of company into Limited Liability Company (LLP) enhanced to include value of assets of the company not exceeding INR 50 million in last three years.
- Applicability of place of effective management provision based residency rules deferred by one year.
- Tax incentive on employment generation proposed to be extend to all sectors subject to conditions.
- TDS provisions on brokerage and commission rationalized.

Indirect Tax proposals

Krishi Kalyan Cess

- Krishi Kalyan Cess is proposed to be levied on any or all the taxable services at the rate of 0.5% of the value of taxable services w.e.f 1 June 2016.

Banking

- Banks and other financial institutions including NBFCs providing services by way of extending deposits, loans or advance will be allowed to reverse credit in respect of exempted services on actual basis in addition to 50% reversal.

Insurance

- Services provided by Insurance Regulatory and Development Authority (IRDA) of India exempted from service tax.
- Services of general insurance business provided under 'Niramaya' Health Insurance scheme launched by National Trust for the Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disability in collaboration with private/ public insurance companies exempted from service tax.
- Service tax liability on single premium annuity policies prescribed at 1.4% of the total premium charged, in cases where the amount allocated for investment or savings on behalf of policy holder is not intimated to the policy holder.
- Services of life insurance business provided by way of annuity under the National Pension System regulated by Pension Fund Regulatory and Development Authority of India exempted from service tax.

Capital markets

- Services provided by Securities and Exchange Board of India (SEBI), by way of protecting the interests of investors in securities and to promote the development of, and to regulate, the securities market exempted from service tax
- Services provided by mutual fund agents/distributor to a mutual fund or asset management company are put under forward charge, i.e. the service provider is liable to pay service tax.

General

- Time limit to issue a show cause notice in cases not involving fraud, collusion, etc. is increased from 18 months to 30 months.
- Interest rates on delayed payment of duty/tax across all indirect taxes is proposed to be made uniform at 15%
- Interest rate in cases where tax is collected but not deposited will be 24% p.a.
- The monetary limit for launching prosecution is increased to Rs. 2 crores of service tax evaded.
- Indirect Tax Dispute Resolution Scheme, 2016 is proposed for all service tax assessees
- Annual return needs to be filed by a provider of output services for each financial year, by the 30th day of November of the succeeding year.

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