



**BUDGET  
ANALYSIS**  
IMPACT ON FINANCIAL SERVICES



## Foreword

The Indian economy ended the last fiscal on a high with growth for the full year touching 7.6% amidst a struggling global economy and a worsening investment climate. In the current fiscal, the domestic economy has continued to show resilience even in the wake of deteriorating global conditions and increased protectionist measures.

The ongoing fiscal can be seen as the year where a number of game changing initiatives were agreed upon such as the passage of the constitutional amendment bill for GST and Bankruptcy code bill. Notwithstanding demonetization, the economy stands at the cusp of noteworthy changes with a move towards GST and a unified tax regime along with a thrust on greater cash accountability and digitization across payment channels.

The Finance Minister in his Budget speech mentioned that the focus of Transform, Energize, Clean India agenda in the Financial Services sector shall be on building stable and stronger institutions.

The thrust areas of the tax proposals introduced in this budget are on stimulating growth, relief to middle class, affordable housing, curbing black money, promoting digital economy, transparency of political funding and simplification of tax administration. The amendments impacting the Financial Services industry have been provided in this alert.



## Summary

The Finance Minister seems to be rather pleased with the Financial Services sector this year. He has announced a few key reforms like setting up the Long Term Irrigation Fund, Micro Irrigation Fund and Dairy Processing & Infrastructure Development Fund. Further, additional INR 80,000 million has been allocated to complete ten million houses under the Pradhan Mantri Awaas Yojana – Gramin, increasing the total fund allocation to INR 230,000 million. Affordable Housing has been reclassified under “Infrastructure” and conditions for tax holiday for the same have been rationalised on a pan-India basis. On the stressed assets front, legal framework has been strengthened and INR 100,000 million has been set aside to re-capitalise banks to deal with stressed assets. On direct tax front, taxation of JDA has been streamlined.

## Key Highlights

Relief for FII investors in case of indirect transfer



Tax and regulatory boost for affordable housing

Tax treatment of JDAs rationalized



Anti-abuse provisions dealing with receipt of property for nil / inadequate consideration widened

Clarification on tax treatment of rupee denominated bonds



BEPS Action Plan 4 introduced

# Policy Update

## Foreign Direct investment

- Foreign Investment Promotion Board (FIPB) proposed to be abolished in 2017-18. Detailed plans will be announced in due course
- Further liberalization of FDI policy is under consideration

**Impact:** Will result in ease of doing business in India

## Commodities exchange

- Expert committee will be constituted to study and promote creation of an operational and legal framework to integrate spot market and derivatives market in the agricultural sector, for commodities trading. e- NAM to be an integral part of the framework
- Commodities and securities derivative markets will be further integrated by integrating the participants, brokers, and operational frameworks

**Impact:** Proposed integration is likely to benefit the farm community, consumers and other stakeholders

Affordable housing is a priority for this Government and it was expected to get an Infra Status. With the Infra status, developers can access foreign funds at a cheaper cost by way of debt and will be a priority lending for banks as well. This should result into a progress in the said sector

# Policy Update

## Securities exchange

- Process of registration of financial market intermediaries like mutual funds, brokers, portfolio managers, etc. will be made online by SEBI
- Systemically important NBFCs regulated by RBI and above a certain net worth, to be categorised as Qualified Institutional Buyers (QIBs). This will strengthen the IPO market and channelize more investments
- SEBI, RBI and CBDT will jointly put in place necessary common systems and procedures for registration, opening of bank and demat accounts and issue of PAN for Foreign Portfolio Investors (FPIs)
- Individual demat accounts to be linked with Aadhaar

**Impact:** Will result in ease of doing business in India

## Other Measures

- Security Receipts (SR) issued by a securitisation company or a reconstruction company under the SARFAESI Act will be permitted for listing and trading on stock exchanges

**Impact:** This will provide an entry and exit opportunity to investors in SRs and enhance capital flows

- Bill to curtail menace of illicit deposit schemes, Ponzi schemes etc. will be introduced. A bill relating to resolution of financial firms will be introduced.

**Impact:** This will contribute to stability and resilience of our

financial system

- A mechanism to streamline institutional arrangements for resolution of disputes in infrastructure related construction contracts, PPP and public utility contracts will be introduced as an amendment to the Arbitration and Conciliation Act 1996

**Impact:** Quick resolution of disputes to boost infra funding and encourage PPP arrangements in infra sector.

- To safeguard integrity, stability of the Financial Sector and enhance cyber security, the Computer Emergency Response Team (CERT-Fin) will be established. CERT – Fin will coordinate its activities with financial sector regulators and other stakeholders

**Impact:** This is to enhance confidence of stakeholders in the Government's push for Digital India.

- Payments Regulatory Board is to be constituted replacing the existing Board for Regulation and Supervision of Payment and Settlement Systems. The proposed Board to have equal representatives from within RBI and the Government of India. The powers and functions of the Payment Regulatory Board to be prescribed.

**Impact:** measure to ensure transparency in regulating the Payment and Settlement Systems.

- The proposed amendments to the Securities and Exchange Board of India Act, 1992 (SEBI Act) are related to the Securities Appellate Tribunal (SAT) under the SEBI Act.

Particulars	Securities and Exchange Board of India Act, 1992	
	Existing provisions	Proposed changes under the Finance Bill, 2017
Number of SAT	Possible to have 1 or more SAT	Only 1 SAT
Jurisdiction of SAT	No provision to set up jurisdictional Benches	SAT may have 1 or more jurisdictional benches
Members of SAT	Presiding Officer and 2 members to be determined by Central Government	Presiding Officer, Judicial Members and Technical Members to be determined by Central Government

**Impact:** Structural changes in the constitution of SAT by inclusion of judicial members and technical members to ensure that the decisions are balanced from point of view of sector specialties and legal expertise and experience.

# Direct Tax

## Banking & securities

- It is proposed to extend benefit of section 43D Income-tax Act, 1961 ("Act") to co-operative banks. Thus, co-operative banks will be taxed on interest income in relation to certain categories of bad and doubtful debts, in the previous year in which it is credited to profit and loss account or actually received, whichever is earlier. Consequently, the deduction of interest expense will be allowed in the hands of the payer on payment basis.
- Deduction under section 36(1)(vii) of the Act in connection with provision for NPA increased from 7.5% to 8.5%.
- It is proposed to provide that any person as referred to in clause (23AAA), Investor Protection Fund referred to in clause (23EC) or clause (23ED), Core Settlement Guarantee Fund referred to in clause (23EE) and any Board or Authority referred to in clause (29A) of section 10 of the Act shall be mandatorily required to furnish a return of income.

## Investment management

- Provisions of indirect transfer shall not apply to investors of Foreign Institutional Investors (FIIs) which are registered as Category I or II with the Securities and Exchange Board of India.
- It was mentioned in the budget speech that a separate clarification will be issued that indirect transfer provision shall

not apply in case of redemption of shares or interests outside India as a result of or arising out of redemption or sale of investment in India which is chargeable to tax in India.

- Conversion of Compulsorily Convertible Preference Shares (CCPS) into equity shares will be specifically tax exempt with effect from 1 April 2018. Further, the holding period of such equity shares will date back to when the shares were first acquired as CCPS. The cost of acquisition of such equity shares will also be the same as the cost of acquisition of CCPS.

There is a commitment in the Memorandum to protect genuine cases and also notify transfer for which the condition of chargeability to STT on acquisition shall not be applicable. A notification in this regard as soon as the proposals are accepted but before the new legislations comes in force would be ideal to protect the interest of genuine investors.

- For the purpose of safe harbor provisions for investment funds under section 9A of the Act, the requirement of average

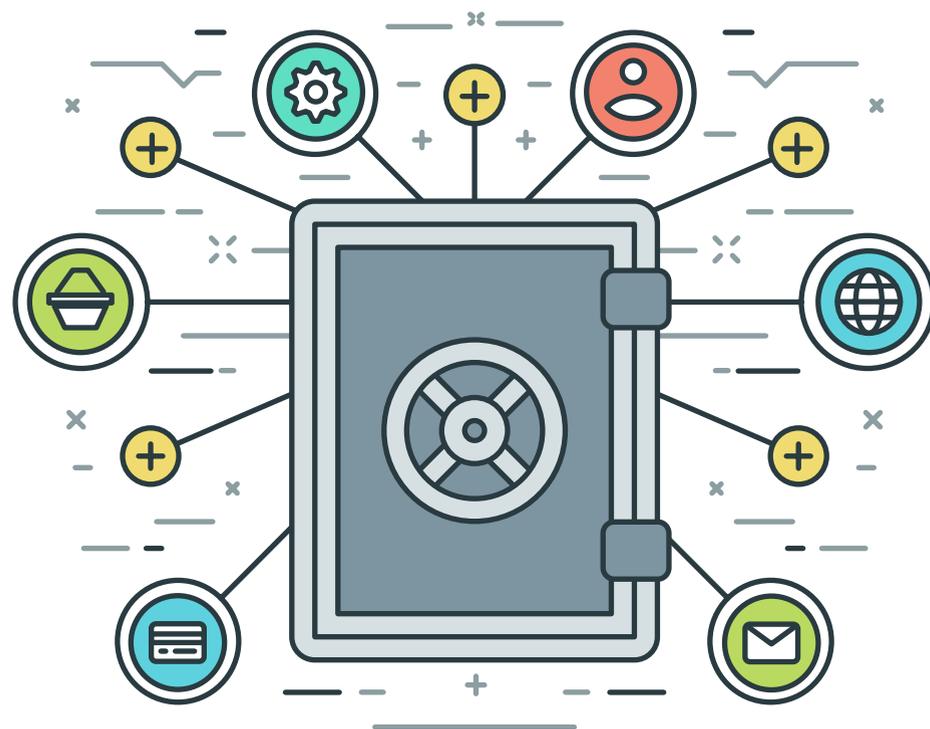
monthly corpus of INR 1,000 million for an investment fund shall not apply in the year of winding up. This shall apply with retrospective effect from 1 April 2016.

- Units received by a unit holder under a consolidated plan of mutual fund shall enjoy the holding period of the units given up in such consolidation scheme. Further, the cost of the units received will be the same as the cost of the units given up under such consolidation scheme.
- Transfer of "rupee denominated bond" but issued outside India by Indian company, from one non-resident to another shall not be regarded as a taxable transfer.
- Foreign exchange gain arising at the time of redemption of rupee denominated bonds which was allowed to be ignored in case of primary/initial subscribers is now allowed to be ignored in the hands of any subsequent acquirer of such rupee denominated bonds
- It is proposed to extend the concessional rate of TDS of 5% on interest payment in respect of external commercial borrowings made before 1 July 2020. The benefit of 5% TDS is further extended to interest payable on rupee denominated bonds (masala bonds) issued outside India before 1 July 2020. This is with retrospective effect from 1 April 2016.
- It is proposed to extend the concessional rate of TDS of 5% on interest payable before 1 July 2020 to FII and QFI on their investment in Government securities and rupee denominated

# Direct Tax

corporate bonds provided the rate of interest does not exceed prescribed limits.

- Tax on dividends @ 10% in the hands of the recipient which was earlier taxable for individuals, Hindu Undivided Family (HUF) and Firms receiving dividends of more than INR 1 million, is now extended to all recipients except for domestic companies, charitable, religious, educational institutions, hospitals as mentioned under section 10(23C), domestic companies and trusts registered under section 12AA of the Act. Other trusts such as private trusts, investment trusts brought under tax net.



- If the consideration for transfer of shares of a company (other than shares listed on recognized stock exchange and traded regularly) is less than the Fair Market Value determined in the manner prescribed, the FMV shall be deemed to be the full value of consideration for tax purposes
- Exemption on sale of long term listed shares will now be restricted to those shares where STT was paid at the time of acquisition on or after 1 April 2004. However, exemption from the said tax shall be prescribed by way of a separate notification to cover cases like IPO, FPO, bonus, right issue.
- Scope of section 56 of the Act has been widened to cover receipt of sum of money, any property, or any immovable property by a person from any other person (i.e. all categories of tax payers included) without consideration or for inadequate consideration in excess of INR 0.05 million

## Real Estate

- Joint development agreement
  - In case of an individual / HUF who transfers land or building or both under a Joint Development Agreement (JDA), capital gains in the hands of such individual / HUF (landowner) shall be chargeable to tax in the year in which the completion certificate for the whole or part of the project is issued by competent authority.
  - The stamp duty value of the landowner's share in the project on the date of issuing of completion certificate

and monetary consideration (deemed consideration) received by the landowner shall be considered as the sales consideration for the computation of capital gains taxation under JDA agreement.

- When the landowner sells his share of developed project/ unit (i.e. where deemed consideration is taxed) in future, the difference between actual sales consideration less the deemed consideration on which capital gains was already paid under JDA shall be considered for taxation.
- In case landowner transfers his share of the project on or before issue of completion certificate, the actual consideration shall be taxable in the year of such sale.
- It is proposed to provide one year tax exemption from notional rental income from unsold building or land appurtenant held as stock-in-trade and which has not been let out during the previous year. The period of one year shall be from the end of the financial year in which the construction completion certificate has been obtained from competent authority.
- Period of holding for long term capital gain in case of immovable property held as investment reduced to 24 months from 36 months.
- Set off of loss from house property with other heads of income restricted to INR 0.2 million
- For immovable property, mode of payment has been specified

# Direct Tax

as account payee cheque or an account payee bank draft or by use of electronic clearing system through a bank account.

- Affordable housing  
The existing provisions of section 80-IBA provides for 100% deduction in respect of the profits and gains derived from developing and building certain housing projects subject to specified conditions. The conditions specified, inter alia, include the limit of 30 sq. mts for the built-up area of residential unit in respect of project located in the Chennai, Delhi, Kolkata and Mumbai or within 25 kms from the municipal limits of these four cities.

The following relaxations have been proposed in the said section from AY 2018-19:

- Size of residential unit shall be measured with respect to 'carpet Area'
- The restriction of 30 sq. mtr on size of the residential unit shall be applicable in case of metropolitan cities viz. Chennai, Delhi, Kolkata and Mumbai and 60 sq. mtr for rest of the Country
- The period for completion of the project for claiming deduction is increased to 5 years from 3 years earlier
- It is also proposed vide the Budget Speech that Affordable housing to be given infrastructure status. This could enable the developers to avail priority lending from banks and debt from foreign lenders subject to necessary

amendments under relevant laws.

## Corporate tax

- Corporate tax rate is proposed to be reduced to 25% in case of domestic companies having a total turnover or gross receipts not exceeding INR 500 million. In other cases, the corporate tax rate remains unchanged.
- In case of demerger of one foreign company into another foreign company, where shares of an Indian company are transferred, the cost of shares of the said Indian company in the hands of the resulting company will be the same as the shares first acquired by the demerged company.
- Cost of acquisition for capital asset (including immovable property) acquired before 01 April 2001 shall be allowed to be taken at fair market value as against 01 April 1981. Cost of improvement shall include only those capital expenses which are incurred on or after 01 April 2001.
- Exemption from long term capital gain arising from the sale of long term capital asset (including immovable property), if sale proceeds are invested in bonds notified by Central

Interestingly, contrary to expectations, a banking cash transaction tax (or equivalent) has not been introduced

Government redeemable after 3 years.

- It is proposed to allow deduction of 100% of profits for eligible start-ups for three consecutive years out of seven years (as against five year earlier).
- It has been clarified that any term defined in a tax treaty shall derive its meaning from the tax treaty. Where a term has not been defined in a tax treaty but the Act, it shall have the meaning as ascribed in the Act
- It is proposed to extend the time limit for carry forward of MAT/ AMT credit to 15 years. Further, certain restrictions have been placed for carry forward of MAT/ AMT credit where it includes FTC.
- Time limit for making an assessment order for assessment year 2018-19, is proposed to be reduced from existing twenty-one months to eighteen months from the end of the relevant assessment year. For assessment year 2019-20 and onwards, the said time limit shall be twelve months from the end of the assessment year in which the income was first assessable.
- Time limit for making an order of assessment, reassessment or re-computation under section 147, in respect of notices served under section 148 on or after 1 April 2019 shall be twelve months from the end of the financial year in which notice under section 148 is served.

# Direct Tax

- Provisions proposed to be introduced restricting cash transactions and promoting digital economy.
- Section 115JB is proposed to be amended so as to provide the framework for computation of book profit for Ind AS compliant companies in the year of adoption and thereafter.

## Personal tax

- Income tax rate is proposed to be reduced to 5% from 10% in case of total income of individuals between INR 0.25 million to INR 0.5 million.
- Surcharge @10% introduced where total taxable income exceeds INR 5 million but not exceeding INR 10 million. Surcharge at the rate of 15% to continue on individuals earning total income above INR 10 million.
- It is proposed that partial withdrawal from National Pension Scheme Trust by an employee, not exceeding 25% of his contribution made, shall be exempt from tax upon fulfillment of prescribed conditions. The amendment will be effective from assessment year 2018-19.
- It is proposed that deduction up to 20% of gross total income can be claimed in case of an individual who invests in the National Pension Scheme not being an employee.
- It is proposed to amend section 197A so as to make Individuals and HUFs eligible for filing self-declaration in Form. No.15G/15H for non-deduction of TDS in respect insurance commission referred to in section 194D.

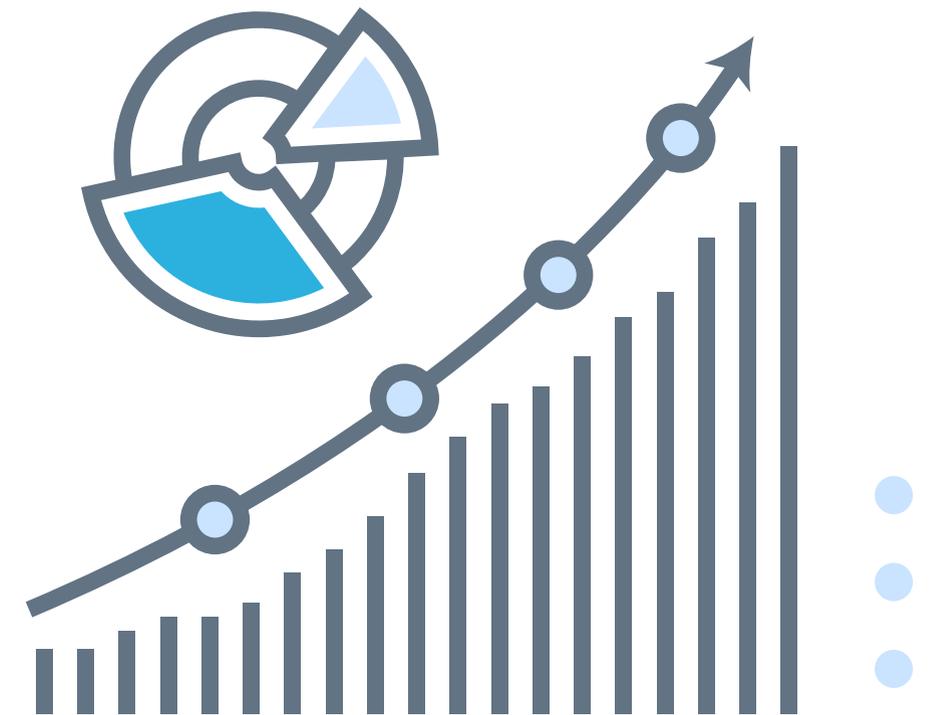
- It is proposed that individuals/ HUFs (other than those covered under 44AB), are required to deduct TDS at the rate of 5% on payment of rent to a resident exceeding INR 50,000 for a month or part of the month.

## Transfer pricing

- Relaxation in domestic transfer pricing compliances
  - With a view to reduce the domestic transfer pricing compliance burden, the scope of applicability of domestic transfer pricing provisions has been relaxed.
  - The definition of specified domestic transactions has been restricted to exclude expenditure payments made by domestic companies to related parties (referred to in 40A(2)(b)) which do not enjoy any tax holiday/profit linked deduction.
  - Domestic transfer pricing provisions will be applicable only if one of the domestic Indian entities involved in the inter-company transaction is enjoying benefits of any tax holiday/profit linked deduction and the aggregate of such transactions exceed INR 200 million. Therefore, where none of the group companies resident in India enjoy any tax holiday/profit linked deduction, the group would be exempted from domestic transfer pricing compliances.
  - This amendment shall take effect from 1 April, 2017 and will be applicable from assessment year 2017-18.
- Introduction of secondary adjustment in the Transfer Pricing

regulations

- To align the transfer pricing provisions with the OECD guidelines and international best practices, concept of secondary adjustment has been introduced. Thereby, the new law removes the imbalance between the actual profit



# Direct Tax

allocation (consistent with the arm's length principle) vis-à-vis the cash account of the taxpayer.

- The tax payer shall be required to carry out a secondary adjustment where the primary transfer pricing adjustment has arisen either from suo-moto action (by assessee), or as made by the assessing officer (accepted by the assessee), or under an advance pricing agreement / or safe harbour rules, or as a result of resolution by way of mutual agreement procedure.
- The excess money available with the associated enterprise consequent to the primary adjustment, if not repatriated to India within the prescribed time, shall be deemed to be an advance made by the taxpayer, requiring imputation of interest income.
- No secondary adjustment shall be made if the amount of primary adjustment does not exceed INR ten million rupees and the primary adjustment pertains to assessment year 2016-17 or before.

## BEPS Action Plan 4

- In line with the recommendations of OECD BEPS Action Plan 4, it is proposed that a new section 94B be inserted to provide that deduction for interest payment exceeding INR 10 million by an Indian company or a permanent establishment of a foreign company to its associated enterprises, shall be restricted to 30% of its EBITDA or interest paid or payable to associated enterprise, whichever is less. For this purpose,

debt shall be deemed to be treated as issued by an associated enterprise where the associated enterprise provides an implicit or explicit guarantee to the lender or deposits a corresponding and matching amount of funds with the lender. This provision is not applicable to banks and insurance companies.

- Excess interest can be carried forward for eight subsequent assessment years.



# Indirect Taxes

## Banking & securities

- Interest or discounts earned by the Banks and NBFCs engaged in providing services by way of extending deposits, loans or advances shall be considered as exempted service for reversal of CENVAT Credit under Rule 6 of CENVAT Rules. [effective from 2 February 2017]
- Import of Micro ATMs (version 1.5.1), miniaturised POS card reader for mPOS (other than Mobile phone or Tablet Computer) and parts & components for manufacture of these devices are exempted from payment of BCD, CVD and SAD. The said exemption is subject to actual user condition. Similar exemption available under Central Excise [effective from midnight of 1 February 2017 / 2 February 2017]
- Exemption on manufacture of Point of Sale [POS] devices and all goods for manufacture of POS devices subject to actual user condition has been extended until 30 June 2017 [effective from 2 February 2017]

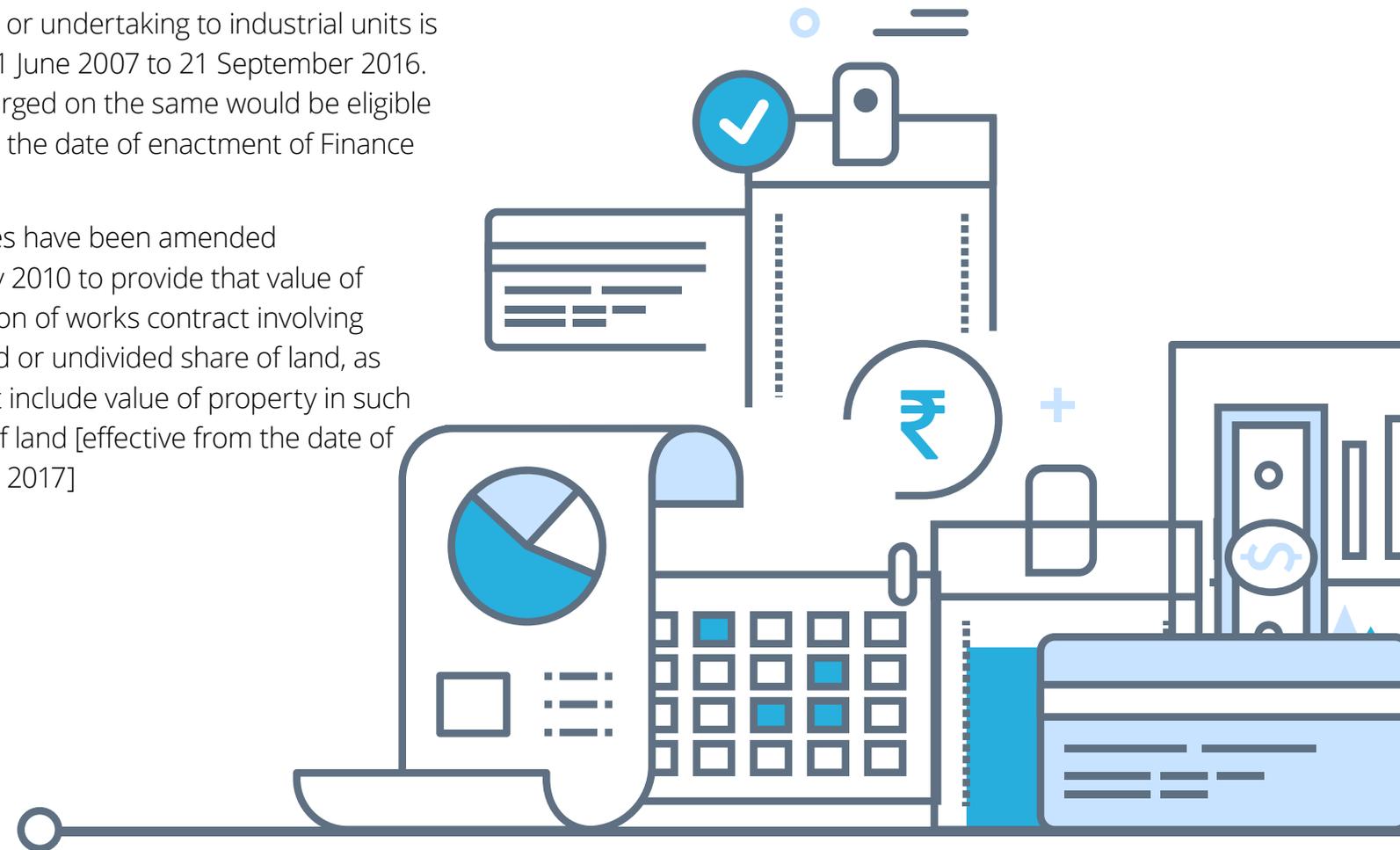
## Life Insurance

- Life insurance services provided or agreed to be provided by the Army, Naval and Air Force Group Insurance Funds to members of the Army, Navy and Air Force, respectively, under the Group Insurance Schemes of the Central Government has been exempted [effective from 2 February 2017]
- The said exemption shall also be applicable for services provided during the period starting 10 September 2004

- to 1 February 2017. Service tax already discharged on the same would be eligible for refund. [effective from the date of enactment of Finance Bill, 2017]

## Real-Estate

- Services provided by way of long-term lease of industrial plots for 30 years or more, by State Government industrial development corporation or undertaking to industrial units is exempted for the period 1 June 2007 to 21 September 2016. Service tax already discharged on the same would be eligible for refund. [effective from the date of enactment of Finance Bill, 2017]
- Service Tax Valuation Rules have been amended retrospectively from 1 July 2010 to provide that value of service portion in execution of works contract involving transfer of goods and land or undivided share of land, as the case may be, shall not include value of property in such land or undivided share of land [effective from the date of enactment of Finance Bill, 2017]



# Glossary

AMT – Alternate Minimum Tax

BCD: Basic Custom Duty;

BEPS – Base Erosion and Profit Shifting

CENVAT Rules: CENVAT Credit Rules, 2004;

CVD: Countervailing Duty;

EBITDA – Earnings Before Interest, Taxes, Depreciation and Amortization

FII – Foreign Institutional Investors

FTC – Foreign Tax Credit

MAT – Minimum Alternate Tax

NPA – Non Performing Assets

OECD – Organisation of Economic Cooperation and Development

QFI - Qualified Foreign Investor

SAD: Special Additional Duty

Service Tax Valuation Rules: Service Tax (Determination of Value) Rules, 2006;



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