Union Budget 2019-20

Capital Market
Corporate Laws
Foreign Investments
Financial Services Sector
Prevention of Money Laundering
Distressed Companies
Infrastructure Sector
Direct Taxes
Start-ups

July, 2019
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SECTION-1
Investment Climate
Budget 2019 determined to retain the attractiveness of India as FDI destination

Proposes amendments in FEMA w.r.t FDI, FPI & NRI

Considering 6% y-o-y growth in foreign investment, Budget 2019 proposed few measures to make India more attractive in an attempt to retain the status of world’s top remittance recipient.

Liberalizing sectoral caps & conditionalities

- **Aviation sector**
  
  - Currently, Air transport services is currently under Automatic up to 49%, Government beyond 49% (Automatic up to 100% for NRIs/ OCIs) in case of following:
    
    - Scheduled Air Transport Service/ Domestic Scheduled Passenger Airline
    - Regional Air Transport Service

  - Further, Foreign airlines are allowed to invest in the capital of Indian companies, operating scheduled and non-scheduled air transport, services up to the limit 49 percent of the paid up capital of the Indian investee company under Government route.

- **Media (animation, Animation, Visual effects, Gaming and Comics sector)**

  - Currently FDI is allowed up to 26% through government route in print media sector for publishing newspaper, periodicals, etc.

- **Insurance sectors**

  - Currently, FDI is allowed up to 49% under automatic route in case of insurance company, insurance brokers, Third party Administrators, Surveyors and Loss Assessors and other Insurance Intermediaries appointed under IRDA Act, 1999.
• It is proposed to permit 100% FDI for insurance intermediaries\(^1\).

**Single Brand Retail sector**

• Currently, In respect of proposals involving foreign investment beyond 51 percent, sourcing of 30 percent of the value of goods purchased, will be done from India, preferably from MSMEs, village and cottage industries, artisans and craftsmen, in all sectors. The quantum of domestic sourcing will be self-certified by the company, to be subsequently checked, by statutory auditors, from the duly certified accounts which the company will be required to maintain. The procurement requirement is to be met in the first instance as an average of five years total value of goods purchased beginning 1st April of the year of the commencement of the business. Thereafter it shall be met on an annual basis. For the purpose of ascertaining the sourcing requirement, the relevant entity would be the company, incorporated in India, which is the recipient of foreign investment for the purpose of carrying out single brand product retail trading.

• Set off against incremental sourcing is available during initial 5 years.

• Sourcing norms will not be applicable up to three years from commencement of the business i.e. opening of the first store for entities undertaking single brand retail trading of products having 'state-of-art' and 'cutting-edge' technology and where local sourcing is not possible. Thereafter, condition mentioned above will be applicable.

• Budget 2019 proposes to ease local sourcing norms.

**Foreign Portfolio Investment in capital instruments:**

• Existing provisions permit aggregate investment by all FPIs to the extent of 24 percent of paid-up equity capital on a fully diluted basis or paid up value of each series of debentures or preference shares or share warrants. Individual limit of investment is 10%.

\(^1\)“intermediary or insurance intermediary” includes insurance brokers, reinsurance brokers, insurance consultants, surveyors and loss assessors [Section 2 (f) of IRDA Act, 1999]
- FEMA (TISPRO) Regulations, 2017 permit increasing the aggregate limit of 24% up to the sectoral cap/statutory ceiling, as applicable, with the approval of Board and approval by way of special resolution from shareholders.

- Budget 2019 proposes to increase the aggregate limit from 24% to sectoral foreign investment limit with the option to the concerned corporates to lower the threshold.

**Foreign Portfolio Investment in other than capital instruments:**

- Budget 2019 proposes to permit FPIs to subscribe to listed debt securities issued by REITs and INvITs.

**Investment by Non-Resident Indian (NRI) under PIS:**

- Currently, as per FEMA (TISPRO) Regulations, 2017 NRIs can invest under Portfolio Investment Scheme subject to 5 percent of the total paid-up equity capital on a fully diluted basis or should not exceed 5 percent of the paid-up value of each series of debentures or preference shares or share warrants issued by an Indian company and the total holdings of all NRIs and OCIs put together shall not exceed 10 percent of the total paid-up equity capital on a fully diluted basis or shall not exceed 10 percent of the paid-up value of each series of debentures or preference shares or share warrants.

- Aggregate ceiling of 10 percent may be raised to 24 percent if a special resolution to that effect is passed by the shareholders of the Indian company.

- In order to have further participation by NRI’s with regard to investment in Indian capital markets, Budget 2019 proposes to merge the NRI – PIS limit with FPI route thereby increasing the ceiling available for investment in Indian entities.

**FDI in PSUs that are part of Emerging Market Index**

In order to have better shareholding of PSUs, Budget 2019 proposes to raise foreign shareholding limits to maximum permissible sectoral cap for such PSUs that are part of Emerging Market Index.
Sea of changes for the Indian Capital Market

The Indian capital market has been performing quite well in the recent times, competing shoulder-to-shoulder with the most developed of economies globally in terms of Return on Investment (ROI). Flagship indices such as Sensex and Nifty are at an all-time high, foreign inflows in the Indian market have increased significantly in the past few years, the mutual fund space has also been very active and innovative fintech solutions bring buying and selling securities at the fingertips of the investor. Sweeping reforms announced by the Securities and Exchange Board of India (SEBI) at regular intervals facilitate transparency and efficient pricing in the market and have made the Indian capital market the apple of the eye of domestic as well as foreign investors.

With the country’s spending pattern experiencing a structural shift as more and more houses choose to invest in financial instruments rather than lock their money in a bank account, the Indian capital market seems poised to maintain its uptrend for a long time. Therefore, given such a pretext, expecting major developments from the Budget does not seem unreasonable. The author in this write-up has attempted to cover the expectations from and the outcome of the budgets. The write-up has been segregated into two segments – a) Equity market and b) Bond market.

**Equity Market:**

Equity markets in India finance major capital requirements of Indian businesses. They have been on a consistent rise over the years. To grow further, it requires constant push and support which the government has been providing through its policies. The market expects to have continued support in the future as well.

**Issuers’ view**

*Background:* Equity market has always been an attraction for the businesses in India. They tend to depend largely on equity to finance their fund requirements. Though, foreign investors are facing hurdles in making investments in equity market due to stringent conditions posed by various laws and policies, however, despite the problems, the statistics reveal that India’s FDI inflows in 2018-19 remained strong at US$ 64.375 billion marking a 6% growth over the previous year. The issuers look forward to measures for further increasing the growth rate of equity market in the wake of ease of business.

*Expectations:* From the Union Budget 2019, the issuers in equity market expected the following:

- Relief from Dividend Distribution Tax
• Easier entry norms for Foreign Portfolio Investors
• Relief in Foreign Direct Investment policies
• Easier procedures for raising funds through equity
• Time-saving and cost-saving measures for issue of equity instruments

Actual: The budget came with the following propositions that the equity market had not foreseen:

• Minimum public shareholding requirement in the listed companies be raised to 35% as against the current threshold of 25%.
• Viability of FDI in aviation, media (animation, AVGC) and insurance sectors will be examined in consultation with all stakeholders.
• 100% Foreign Direct Investment (FDI) will be permitted for insurance intermediaries.
• Relief in levy of Securities Transaction Tax (STT) was proposed by restricting it only to the difference between settlement and strike price in case of exercise of options.

Investors’ view
Background: The investors in equity market have been active in the recent times. However, certain glitches like levy of STT and capital gain taxes tend to put bars on trading by investors in the capital market.

Expectations: The investors only want one thing, i.e. increase in returns earned by them. They expected the budget to address these issues by reducing tax burdens on transactions in securities.

Actual: The budget responded to the calls of investors by restricting levy of STT difference between settlement and strike price in case of exercise of options instead of the entire settlement price. However, no relief was given on trading in equity and other instruments.

Bond Market:
A thriving bond market is very essential for the development of any economy. Usually, in a developing or developed economy, the size of bond market is multiple times its equity market, however, the situation is opposite in India. This disparity is majorly due to unstable interest rates, regulatory uncertainties, investor sentiments etc.

Bond market can be divided into two major categories:

i. Government bonds - bonds issued by the Central government or State governments or any government entity with the objective of financing government schemes, or general needs of the country.
ii. Corporate bonds - bonds issued by corporates to finance their short term and long term fund needs.

However, for this write-up the focus will be on corporate bond market.

In terms of size of the bond market, the Indian market is much smaller than that of its Asian peers. The table below shows the outstanding corporate bonds in some of the select Asian countries:

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<td>Vietnam</td>
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Figures denominated in USD billion

Source: Care Ratings

In terms of market depth, outstanding bonds in the Indian market as percentage of Gross Domestic Product stood at 16% as at the end of FY 19, which still is mediocre as compared other countries in Asia. The figure below depicts corporate bond market’s depth, as of March, 2018.

Corporate bond market depth [Outstanding debt as % of GDP]

Source: Care Ratings

The low depth of the market has always kept the regulators and policy makers concerned, consequently, we have always had reforms in the
budget relating to development of bond markets. This year has been similar as the industry expected several reforms from the regulators. The author of this article has tried to discuss about the expectations from the Budget and the actual outcome.

**Issuers’ view:**

*Background:* Corporates access funds from within India as well as from other countries. Cross-border funding is encouraged by regulators but at the same time, regulatory constraints bar such funding into India. Also, the varied practices regarding stamp duties on debt issuances dull out the attractiveness of investment opportunities in India. Limits on investment by foreign entities and ever-changing regulatory requirements have impacted the market to a negative side.

Recent initiatives such as nudging large corporates to meet 25% of their funding needs through bond markets, considering regulatory recognition for investment in bonds to include A rated bonds as well (in addition to existing stipulations of only up to AA rating) and attempting to introduce uniform stamp duty for issuance of bonds across the country etc. have been positive moves towards growth of the market but further measures are still required.

In the recent years, interest rates have been very high resulting in increased cost of capital for the issuer. It is felt that the requisite foundations for expansions of bond market have been laid and now it is time to focus on methods of reducing cost for the issuers.

Major chunk of issues of corporate bonds is made through the private placement route owing to the relaxed regulatory requirements compared to that of public issue of bonds. Due to this, the bond market remains inaccessible to a wide category of investors.

*Expectations:* Corporates in the bond market expected favourable measures to make the market more accessible.
• Rationalization of FPI investment in corporate debt;
• Streamlining of stamp duty on financial instruments;
• Measures for reduction in cost of capital as well as cost of issue;
• Optimal tax policies and compliance framework for startups and innovative structures.

Actual: The budget focused on deepening the corporate bond market. It came up with several proposals that will facilitate expansion and growth of bond market with specific focus in infrastructure sector. Following are the proposals made in the budget:

• An action plan to deepen the market for long term bonds including for deepening markets for corporate bond repos, credit default swaps etc., with specific focus on infrastructure sector, will be put in place.
• FIIs and FPIs will be permitted to transfer/sell, to any domestic investor, within specified lock-in period, debt securities issued by Infrastructure Debt Fund – Non-Bank Finance Companies (IDF-NBFCs).
• To deepen the corporate tri-party repo market in Corporate Debt securities, Government will work with regulators RBI/SEBI to enable stock exchanges to allow AA rated bonds as collaterals.
• User-friendliness of trading platforms for corporate bonds will be reviewed, including issues arising out of capping of International Securities Identification Number (ISIN).

Investors’ view:

Background: At present, retail investors invest through mutual funds because of the high face value of bonds and absence of tax exemptions. Mutual funds on the other hand are provided with various tax exemptions on investment in corporate bonds.

Short term investments acts as a lubricant to keep the flow of liquidity smooth in the market. Tax implications on short term capital gains prevent the investors from making such investments which hurts the investor sentiment as well as the capital flow in the economy.

Investors in the Indian economy are inclined towards saving but not towards investment. This creates a huge gap between the amount of consumption, savings and investment which disturbs the equilibrium. Their savings needed to be channelized into investments.

Further, surveys proved that uncertainties around economic policies, ambiguity of laws, inconsistent frameworks, arbitrariness in laws etc. also block the way for foreign investments. FPIs tend to scare away from ever-fluctuating compliance norms.

Expectations: Based on the above pretext, the investors expected the following reforms:
- Measures allowing FPIs to subscribe to corporate debt without any issue-wise limit;
- Relaxation of group-wise investment limits for FPIs;
- Having in place a well-defined framework for foreign investments that remains constant;
- Tax incentives to retail investors in corporate bonds;
- Long term capital gain benefits on bonds;
- Equal priority in rationalizing tax implications on short term investments in bonds;
- Innovations enabling liquidity of bonds in secondary market;
- Incentives on investment by way of tax benefits, better returns, low-risk instruments etc.;
- Consistency of laws and frameworks.

Actual: The budget made several propositions that would aid growth of bond markets in India. One such proposition was permitting FPIs to subscribe to listed debt securities issued by ReITs and InvITs.

**Budget propositions that are likely to impact both segments of capital market**

*Focus on foreign investments:* The focus of the budget seemed to be majorly on mobilising foreign investments into the country. In this direction the budget proposed the following:

- to rationalize and streamline the existing Know Your Customer (KYC) norms for FPIs to make it more investor friendly without compromising the integrity of cross-border capital flows.
- organisation of an annual Global Investors Meet in India, using National Infrastructure Investment Fund (NIIF) as the anchor, to get all three sets of global players-top industrialists/corporate honchos, top pension/insurance/sovereign wealth funds and top digital technology/venture funds interested in Indian capital markets.
- merger of the NRI-Portfolio Investment Scheme Route with the Foreign Portfolio Investment Route.

*Other proposals:* It was proposed to initiate steps towards creating an electronic fund raising platform – a social stock exchange - under the regulatory ambit of Securities and Exchange Board of India (SEBI) for listing social enterprises and voluntary organizations working for the realization of a social welfare objective so that they can raise capital as equity, debt or as units like a mutual fund.

This initiative has the potential to enhance growth of capital market and at the same time support social development of the nation.
Infrastructure gets the centre stage in the Budget 2019

Broadly the infrastructure sector is classified into two types, hard and soft. Hard infrastructure are physical networks essential for the functioning of almost all modern industries. It primarily consists of but is not limited to roads, airports, waterways, telecommunications, electricity, power, water supply and sanitation among other utilities. Whereas Soft infrastructure refers to those establishments which help maintain the cultural and socio-economic standards of the country. These include educational and health programs, judicial and law-enforcement agencies, transport services, disasters and emergency services among many others. As such infrastructure sector not only has a crucial impact on economic development (better resources for domestic businesses, attracting FDI etc.) but also has a ubiquitous impact on the quality of our daily lives.

Although infrastructure development is primarily the concern of the Government, public-private initiatives over the year have led to accelerated development in this sector. The infrastructure sector has been of primary concerns of the Budget in recent years. As such this writer, at first states the budget expectations revolving around the different utilities and subsequently remarks them with the actual claims.

Health Care

Background: Healthcare in India comprises of hospitals, medical devices, clinical trials, outsourcing, telemedicine, medical tourism and health insurance. Currently accounting for 6% of the country’s GDP, the healthcare market has potential to increase three-fold to ₹8.6 trillion (US$ 133.44). Some of the earlier initiatives seen throughout were the Pradhan Mantri Jan Arogya Yojna, Ayushman Bharat and Mission Indradhanush in September 2018. Despite being a crucial component of our country both economically and socially, the Indian healthcare sector is fragmented with over dependence on a few institutions. High costs, lack of modern equipments and delay in timely and quality treatment of patients loom large. In addition to that, personal hygiene and cleanliness initiatives need aggressive promotion. Toilet penetration in India is less than 60% compared to some of our neighbouring countries whom have reached 90%. Industry leaders suggest that a high GST rate of 18% on basic bathroom fitting like taps and other sanitary ware are also acting as tailwinds.

Expectations: Prevention being better than cure, better environmental standards are required along with improved medical facilities. Clean
rivers, pollution-free environment, zero open defecation, proper management of solid and liquid waste and environmental awareness among citizens are common and necessary attributes of developed nations. The government must up the ante and activities of Swachh Bharat. Although a complete overhaul of the country’s environmental and healthcare infrastructure is not possible through a year’s budget; it definitely can serve a firm base going forward. The budget can be expected to address the following areas in Healthcare:

- Robust Infrastructure and adequate supplies of beds, surgical instruments and other such for non-critical illnesses.
- Greater availability of health insurances expanding from the current set of 10+ crores household under Ayushman Bharat
- Looking into the nuances and approvals of E-pharmacy laws for better availability of affordable medicines
- Strong vaccination campaigns and incentives and tax breaks for preventative screening & personal hygiene
- Addressing security concerns of doctors given rising instances of violence and aggression against them.

**Actuals:** The budget spoke on the Swachh Bharat Abhiyan, initiated in 2014, under which 9.6 crore toilets were constructed since Oct 2, 2014, enabling 5.6 lakh villages and 95% of cities to be Open Defecation Free (ODF). In upwards of 45,000 public and community toilets have been constructed across 1700 cities, covering more than 53% of India’s urban population. The budget further claimed plans to expand into solid waste management in villages, under the same scheme. Healthcare-wise, tax deduction limit for medical insurance was increased from ₹15000 to ₹25,000. For senior citizens, the limit increased from ₹20,000 to ₹50,000 in addition to a limit of ₹100,000 for medical expenditures on critical illnesses.

**Fact check:** The number of recognized doctors increased from 827,006 in 2010 to 841,104 in 2017.

**Ports, Roads, Airports and other such**

**Background:** The Indian Railways is among the world’s 3rd largest networks of rail. The Indian Railways route length network is spread over 115,000 km, with 12,617 passenger trains and 7,421 freight trains each day from 7,349 stations plying 23 million travellers and 3 million tons (MT) of freight daily. India’s railway network is recognized as one of the largest railway systems in the world under single management.

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4 [https://www.ibef.org/industry/indian-railways.aspx](https://www.ibef.org/industry/indian-railways.aspx)
As of April 2019, India has one of the largest road networks across the world, spanning over a total of 5.5 million km\(^5\). This road network transports 64.5 per cent of all goods in the country and 90 per cent of India’s total passenger traffic uses road network to commute. Existing initiatives like Bharatmala and Sagarmala are in place for developing the country’s connectivity. Bharatmala would help develop national road corridors and highways, while Sagarmala would enhance port connectivity, modernization and port-linked industrialization. Yet still, for a modern economy, large portions of the country remain underserved.

India is currently considered the third largest domestic civil aviation market in the world. India has become the third largest domestic aviation market in the world and is expected to overtake UK to become the third largest air passenger market (both international and domestic) by 2024 as per International Transport Association (ITA). However, the Indian Aviation sector is going through one of its toughest phases given the grounding of Jet Airways’ operations. Also, high operating costs like taxes, fuel charges, landing & parking rates has consequently pushed up ticket fares which has made things worst.

Expectations: Although we are quite above the global average, why are there so many mundane issues that are faced by daily farers? Primarily owing to two reasons; First, a lack of maintenance and upkeep of the existing infrastructure and second, an overwhelming population. The aviation sector in spite of competitive pressures has tried to make air travel more affordable and accessible to the wider demographic through the UDAN (Ude Desh ka Aam Nagrik) scheme launched in October 2016. However, key issues need to be addressed if the government seeks to achieve the target figure of 1-billion-flights-per-year. Infrastructure development is key to realizing PM Narendra Modi’s vision of making India a $5 trillion economy by 2024. The following chart lists some of the major concerns:

Continued allocation to construction of highways, roads and expressways across the country

Introduction of more trains on more routes and ways to fast track station redevelopment across major cities.

Financial push to development of the 35 multimodal logistic parks considered by the govt. and private sector participation in logistics.

Consider lowering high taxation on aviation fuel and greater inclusion of UDAN (Ude Desh ka Aam Naagrik)

Finding customized, long-term and cheaper funding for shipping and aircraft finance

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\(^5\) https://www.ibef.org/industry/roads-india.aspx
**Actuals:** The government estimated that railway infrastructure would require an investment outlay of ₹50 lakh crore between 2018-30. In comparison to the current capital outlay of 1.5 to 1.6 lakh crores per annum, completing the stipulated projects would take decades. As such, public-private partnerships are proposed for faster development. The budget also iterated that railways will be encouraged to invest more in suburban railways through Special Purpose Vehicle (SPV) structures like the Rapid Regional Transport System proposed on the Delhi-Meerut route. A programme for railway station modernization was also proposed. Further, New Metro Rail Projects for a total route length of 300 kilometres have been approved during 2018-19. Also, during 2019, about 210 kms of metro lines have been operationalized. With this, 657 kms of Metro Rail network has become operational across the country.

It was also stated that a high pace of road construction at around 130 to 135 km per day was implemented in the last 1000 days. Given the commitment to sustainable development, 30,000 kms of PMGSY roads have been built using Green Technology, Waste Plastic and Cold Mix Technology, thereby reducing carbon footprint. A further upgrade of 1,25,000 kms of road is envisaged over the next five years, with an estimated cost of ₹80,250. Also, existing initiatives like Bharatmala, Sagarmala are being increasingly pushed to develop physical connectivity.

The budget having acknowledged the country’s large domestic aviation market stressed importance on aircraft financing and leasing activities within the country’s shores. Given that foreign entities currently enjoy the profitable gap in aircraft leasing in our country, the government initiated project Rupee Raaftar with the aim to gain through the increasing demand and non-availability of own sources aircraft financing. The government in such regards plans to implement essential elements of the regulatory roadmap to facilitate such activities, the details which can be found [here](#). Proposing to leverage India’s engineering potential, the government also proposes to enable an ecosystem of Maintenance, repair and Growth (MRO) industry to achieve self-reliance in the aviation industry.

Fact Check: India’s passenger (domestic & international) traffic grew at 16.52 per cent year on year to reach 308.75 million in FY18.

**Power & Electricity**

*Background:* The pinnacle of achievements in the power sector over the last five years has been providing electricity to over 96% households. The next focus is electrification of every house. Various policy initiatives were taken to ensure this last mile connectivity. The trend is expected to continue this year. The efforts came to fruition under the *Deendayal Upadhyaya Gram Jyoti* scheme, launched in 2014-15 with...
the aim of taking connections to distant and difficult terrains. Industries have also been given tax rebates to encourage production of renewable energy. The government has set a target of installing 175 GW of renewable energy capacity by the year 2022. 'Saubhagya yojana' was launched by the Prime Minister on 25th September, 2017 with the aim of providing free electricity connections to all households in rural and urban areas.

**Expectations:** A majority of the industry stakeholders anticipate tax reduction, lower rates of interest and subsidies heading into 2019-20’s Union Budget. The initial target of the Saubhagya Yojna was to produce 100 per cent household electrification by 31 December 2018. However, the aim could not be entirely realized due to greater finances required to meet added connections in far-off rural areas. The renewable energy sector although available for various tax exemptions and concession, needs further stimuli if India is to make the shift to clean energy. Budget provisions for charging and storage infrastructure which helps fully utilize renewable energy are also expected. India has 348 gigawatt (GW) installed capacity against peak load demand of 170 GW, even then about one crore households have no access to electricity. Also, the All India Power Engineers Federation (AIPEF) have made public requests to bring electricity under the ambit of the Goods & Services Tax (GST). However, this move may not entirely viable for all sections of the population. Under GST, the cost of such an essential will be passed on to consumers. This may not be desirable to many.

**Actuals:** The budget proposed many initiatives to promote efficiency and growth in the power sector. Among the first mentions was the existing ‘One Nation, One Grid’ model to ensure power availability to states at affordable rates. Blueprints for gas grids, water grids, i-ways and regional airports were also proposed. An outlay of ₹10,000 crore for a period of 3 years was commenced from April, 2019 to encourage faster adoption of electric vehicles. Incentives on purchase of electric vehicles and establishing the necessary charging infrastructure is expected to ease adoption. The government also lowered the GST rate on electric vehicles to 5% from 12% in such regards. The government also aims to provide additional income tax deduction of ₹1.5 lakh on interest paid on loans taken to purchase electric vehicles. Touching upon efficiency, the High Level Empowered Committee (HLEC) recommended retirement of old and inefficient plants and low utilisation Gas plant capacities due to paucity of natural gas. The budget also stated that a package of power tariff and structural reforms would also be announced soon.

On electrification and clean cooking, the government announced provision of more than 7 crore LPG connections among others. Under the UJALA Yojana, a programme of mass scaling up of LED bulbs led to the distribution of 35 crore LED bulbs leading to a cost saving of
₹18,341 crore. It also claimed that all villages and almost 100% households across the country have been provided with electricity.

Fact Check: India’s rank jumped to 24 in 2018 from 137 in 2014 on World Bank’s Ease of doing business - "Getting Electricity" ranking

**Education**

*Background:* According to the Indian Brand Equity Foundation, India has the world’s largest population of about 500 million within the age bracket of 5-24 years which provides a great opportunity for the education sector. Another study found that by 2020 the average age in US will be 46, 42 in Europe, 48 in Japan and only 27 in India. Number of colleges and universities in India reached 39,050 and 903, respectively in 2017-18. India had 36.64 million students enrolled in higher education in 2017-18. Gross Enrolment Ratio in higher education reached 25.8 per cent in 2017-18. This means India is in line to reap the huge demographic dividend which can boost the country’s economy. But this can only be the case if today’s youth are provided the correct skills to help them for the future. Low enrolment, rising costs and high dropouts act as tailwinds. The Govt. budget must have a strong take on the Education sector if it seeks to raise its current gross enrolment ratio to 30% by 2020.

*Expectations:* Although schemes like Samagra Siksha (an overarching programme for the school education sector extending from pre-school to Class 12), Mid-Day Meals and Saakshar Bharat are in place, clearly more can be done. The Union Budget 2018-19 earmarked only Rs. 36,322 crores for programmes under Samagra Shiksha Abhiyan, which was dubbed as too meagre an allocation in the face of depleting teachers training institutes (DIETS - District Institute of Education and Training) and increasing proportions of untrained teachers. There are 6, 22,060 sanctioned posts of teachers in government secondary schools at the national level and only about 76 per cent teachers are in position. As per UNDP Human Development Indices & Indicators, government expenditure as a percentage of GDP was a meagre 3.8% during 2012-17, given the world average of 4.8%. Public expenditure on education as a percentage of GDP in developed countries like the US, UK and Australia was greater than 5%. We believe the following reforms are the need of the hour:

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*Gross Enrollment ratio is defined as the ratio of the total no. of entrants (usually at primary school level) by the total no. of eligible entrants in the country’s population.
Actuals: The government claimed recognition and improvement of various schemes for education in this year's budget. One such was the SWAYAM initiative, a repository of massive online open courses which helped to bridge the digital divide for the disadvantaged sections of the society. Global Initiative of Academic Networks (GIAN) programme was started to upgrade the quality of teaching by tapping the global pool of scientists and researchers. Higher educational institutions are being increasingly encouraged to becoming centres of innovation.

The FM also stated an interesting statistic in that there was not a single Indian institution in the top 200 in the world university rankings five years back. However, presently three institutions – two IITs and IISc Bangalore are in the top 200 bracket. To sustain such trend the budget proposed an outlay of ₹400 crore under the head “World Class Institutions” for FY 2019-20, more than three times the revised estimates for the previous year. Further under the ‘Pradhan Mantri Kaushal Vikas Yojana’ initiative, the government enables about 10 million youth to take up industry relevant skill training. Demographic trends worldwide show that major economies will face severe labour shortages in the future. As such, the focus will be on preparing our youth to take up new age skills like Artificial Intelligence, Big Data, Internet of Things (IOT), 3D Printing, Virtual Reality and Robotics which will be highly valued both within and outside the country.

The government is also focussing on awareness of sports as an integral part of wellness, through the Khelo India Scheme launched in October, 2017. The Government assures commitment to expand the scheme and provide all the necessary financial support. Further, a National Sports Education Board for Development of Sportspersons would be set up under the scheme to popularize sports at all levels throughout the country.

Fact Check: India has become the second largest market for e-learning after the US. The sector is expected to reach US$ 1.96 billion by 2021 with around 9.5 million users.
SECTION-II
Banking & Non-Banking Finance
Banking sector reforms in Budget, 2019

An economy without an effective banking system is a handicapped economy, therefore, an effective banking system is not just a desire but a necessity for every economy. India has a robust banking system and entire money circulation in the economy is handled through the banks. However, from time to time, scams and major defaults have kept on bothering the banking sector.

In order to deal with the increasing number of defaults, the Insolvency and Bankruptcy Code, 2016 was introduced, with the aim of swift resolution of distress in the accounts.

Considering the importance of the sector, every Budget has something or the other to offer, either in the form of recapitalisation or as tax sops for ease of doing business by the banks. Based on the past record, the like every year, the industry had expectations this year as well and in this article the author as tried to discuss what the expectations were and the hits and misses in the Budget.

Fund Allocation to Public Sector Banks

Background: Public sector banks have played an important role in the economic growth and development of the country. They help in mobilising resources from far flung rural areas as well as extending banking services to the remotest parts of the country. PSBs account for almost 70% of the banking activity of the country and thus to maintain its credibility, Government must re-capitalise the PSBs regularly. In the financial year 2018-19, the Government infused nearly Rs. 1,06,000 in the PSBs which was much higher than the provision of Rs 65,000 made in December 2018.

Some factual data with respect to banking companies have been produced below:

- Re-capitalization has worked its way out and the capital infusion has resulted in improvement in the performance of PSBs in the financial year 2018-19. However, Gross NPA ratio of PSBs have remarkably decreased from 15.5% to 13.95 in the duration of March 2018-December 2018. The stressed asset (SA) ratio of PSBs decreased from 16.3% to 14.4% during the same period.
• Gross NPA ratio of Scheduled Commercial banks (SCBs) has declined from 11.5% to 10.1% in the duration of March 2018-December 2019. The restructured standard advances (RSA) ratio has declined from 0.7% to 0.4% during the same period. The ratio of stressed assets decreased from 12.1% to 10.5% during the same period. ROA of SCB’s took a downward leap from 0.21% in the FY 2017-18 to 0.03% in 2018-19 while their ROE declined from 2.34% to 0.4% during the same period.

Expectations: The fund allocation to public sector banks is crucial for the banks that are into deep crisis due to rising bad loans, delays in resolution of large cases under the insolvency and bankruptcy code and liquidity crisis. To meet regulatory capital requirement, government was expected to allocate Rs. 30,000 crores to public sector banks in the budget. Other reforms relating to taxation reforms which would support and improve the position of banks were expected.

Actual: Further capitalisation of Rs 70,000 crore (higher than the expected allocation of Rs. 30,000 crore) has been proposed with an aim to strengthen the credit to stimulate the economy. This concept of
optimum re-capitalisation of the PSBs has enabled stabilisation of the capital structure of an economy.

Facts:

- NPAs of scheduled commercial banks (SCBs) have reduced by over 1 lakh crore over the last financial year. Gross NPA ratio of PSBs is in a reducing spree year over year. Re-capitalisation plays an important role in achieving this success.
- Provision coverage ratio is now at its highest in seven years. This indicates the extent of funds kept aside by banks to cover losses due to bad loans. The cushion is maintained to absorb losses and thus higher the ratio, higher is the absorption of losses and lower is the unexposed part of the bad debts. This indicates better financial health of the economy.
- By way of consolidation, government has smoothly reduced the number of public sector banks by 8.
- Six PSBs have been enabled to recover out of the Prompt corrective action framework. A stitch in time saves nine. This framework helps banks in distress to restore their financial health before they slip into more trouble.

Cash-less economy: Digital India

Background: Cash-less economy is a dream for the new India in making. It has been two years since demonetisation went live to foster the concept of digital India. Several measures that have been taken to encourage this concept being Real Time Gross Settlement (RTGS), National Electronic Funds Transfer (NEFT), IMPS, National Automated Clearing House (NACH), Cheque Truncation System (CTS), mobile wallets, Prepaid Cards (PPI), UPI and the Point of Sale transactions using credit and debit cards. The performance of these measures for the year 2018-19 adds up to 11.8 billion. However, it is believed that still more than 90% of the transactions are cash dominated.7

Expectations: Major expectation in the upcoming budget was to encourage cash-less economy. The policies guiding cashless economy have been in place, but still a lot of dealings in cash are taking place. So new effective policies were expected to be introduced by the government in response to the gruelling issue.

Actual:

- Ease of living has been given significant importance in the making of digital India. With the view to achieve the long term goal of formation of digital India, technology has been largely updated by making personal loans available online, providing doorstep banking facilities to bring more customers on-board and move to the path of

cash-less economy. The customers of one Public Sector Bank are enabled to access services across all Public Sector Banks.

- To subside the cash dominated transactions, Tax deduction at source (TDS) of 2% is levied on cash withdrawal exceeding Rs 1 crore in a year from a bank account.

To promote digital payments, business establishments with annual turnover more than 50 crore are to offer low cost digital modes of payment to their customers and no charges or Merchant Discount Rate to be imposed on customers as well as merchants. RBI and Banks are to absorb these costs from the savings that will accrue to them on account of handling less cash as people move to these digital modes of payment.
What’s in store for affordable housing and housing finance?

There is a direct nexus between an emerging economy and the development of the housing sector. Housing is an indicator of growth and social well-being of an economy. One of the biggest challenges to the development of the housing sector is access to finance. Affordable housing is that part of the housing sector which caters to the section of the society whose income is below the median household income. Broadly, they are divided into two groups, Middle Income Groups (MIG) and Lower Income Group (LIG).

Affordable housing sector has seen a prolonged congestion in the pathway to growth. With regulatory measures such as introduction of Real Estate (Regulations & Development) Act, 2016, Goods and Services Tax (GST), the Government intended to bring in transparency in the sector. There have also been initiatives taken by the Government for boosting the growth of the Housing sector.

While this write-up aims to discuss about what the expectations from the Budget and how they have fared in the Budget, but before coming on to the point let us have a quick recap about reforms which have already been formulated so far.

Reforms formulated so far

Affordable Housing Fund

The Union Budget 2018-19 highlighted the establishment of Affordable housing fund (AHF) in National Housing Bank (NHB) to be funded from priority sector lending shortfalls and bonds authorised by the Government of India. The scheme was expected to contribute towards the growing demand of the sector.

The National Housing Bank issued a refinancing scheme under Affordable Housing Fund\(^8\) with the objective of refinancing the individual housing loans sanctioned and disbursed on or after 1\(^{st}\) April, 2017 falling under rural/urban category based on the demands received from the Primary Lending Institutions.

The individual housing loans eligible for refinancing for urban category was set at an annual household income not exceeding Rs. 6 Lakhs and for rural category, the loans disbursed to (i) the weaker sections as

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defined in the RBI’s priority sector guidelines, (ii) Annual income not exceeding Rs. 3 Lakhs and (iii) Loans disbursed to Women.

The credit-linked subsidy scheme (CLSS), being an integral component of the HFA scheme, was expected to be an aid for the eligible customers providing interest subsidies upto 6.5%. The scheme has been proven to be successful and was extended till March, 2019 and further extended till March, 2020. The total subsidy released till date, including economically weaker section (EWS) Low income group (LIG) and Middle income group (MIG) has been Rs.4454.48 crores.9

Pradhan Mantri Awas Yojana (PMAY)

As a part of the National Mission for Urban Housing and Pradhan Mantri Awas Yojna (PMAY), the Government introduced Housing For All (HFA) intending to facilitate as many as 2 crore dwelling units over several years upto 2022. So far 4,427 cities/towns have been included under PMAY (U). The duration of the Mission is seven years (2015-16 to 2021-22) and has four components: Slum Redevelopment, Credit Linked Subsidy Scheme, Affordable Housing in Partnership with public or private sector and Beneficiary-led individual house construction/enhancements.

The status as on 1st July, 2019 of the houses sanctioned under PMAY for the urban sector reaches to a figure of 84 Lakh compared to the target demand of 100 lakhs, the growth rate in sanctions as compared to 79 lakh houses sanctioned till Q4 of 2018-19. The trend of the growth in sanctions is provided below:

![Graph showing growth in sanctions under PMAY](http://mohua.gov.in/upload/uploadfiles/files/0-%20NHB.pdf)

The trend is likely to reach its target of 100 lakh houses sanction by December 2020. According to Census, the projected per cent of

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country’s population to live in urban areas is to double in a span of 20 years at an estimate of 600 million.

**Expectations from Budget 2019**

Major expectations from budget 2019 for the Affordable housing sector were:

- **ECB routes for Real Estate:** As per the Reserve Bank of India (RBI) policy on ECBS\(^\text{10}\), housing finance companies are included in the eligible borrowers list for the purpose of ECB. The end-use provisions for ECBs have also excluded affordable housing, industrial parks, integrated townships, SEZs from the negative list for all tracks for the end-use provisions. Hence, it was expected that Budget 2019 would highlight the ECB route of funding for real estate better than scheduled commercial banks and NBFCs for long term capital funding option.

- **Increase in demand for affordable housing:** The Budget 2019 was expected to boost the demand for affordable housing as despite much of the efforts, conversion of the demand into actual sales have been at a low rate. One of the key expectations from the Budget 2019 was to increase in the eligibility of CLSS scheme. The dual effect of increase in the interest rate subsidy and GST rate benefit could have proved to be beneficial in increasing the demand for affordable housing.

- **Land acquisition:** It was expected that the Budget 2019 would provide for removing the hindrances in land acquisition, which continued to be a major reason for blockage in the development of the real estate sector. Unavailability of land is a major hurdle in the implementation of various real estate projects. Measures which streamline and synchronise the approach of Central and State Government towards land acquisition will prove to be a boost in growth of the real estate sector.

- **Increase in tax benefit on home loans:** Increase in the deduction limits for interest on housing loans was also expected from the Budget.

**How the Budget turned out to be**

With the Government continuing its thrust for affordable housing and trying hard to recover the moribund real estate sector, there has been a consistent focus towards affordable housing in the budget 2019.

The major changes brought in by the Budget 2019 are summarised as below:

\(^{10}\) [https://rbi.org.in/Scripts/NotificationUser.aspx?Id=11267&Mode=0](https://rbi.org.in/Scripts/NotificationUser.aspx?Id=11267&Mode=0)
1. **Proposal for shift of Regulatory Authority of housing sector from NHB to RBI:** To promote efficient and conducive regulatory environment for the housing sector, to alleviate the NHB from a conflicting mandate due to regulating as well being the refinancer and lender, the Government proposed to return the regulatory authority over the housing finance sector from NHB to RBI.

This said proposal is a long discussed proposal and would help the state of housing finance in the country. Most importantly, NHB will now be able to focus solely on its promotional and refinancing roles. With the ambitious “Housing for all” by 2022, the shifting of regulatory authority to RBI, can be seen as move towards a green signal for entry in the housing finance sector.

This matter has been discussed at length earlier in this booklet.

2. **Increase in tax benefit on home loans:** As was the expectation of the Housing sector, the Government has delivered an increase in the tax benefit by allowing an additional deduction of Rs. 1.5 Lakhs on the interest paid on home loans, by insertion of section 80EEA in the IT Act. The above deduction is subject to following conditions:

   (i) Loan has been sanctioned by a financial institution during the period beginning on 1st April 2019 to 31st March, 2020
   (ii) The stamp duty value of house property does not exceed Rs. 45 Lakhs.
   (iii) Assessee does not own any residential house property on the date of sanction of loan

The above is seen as a welcome move of the government, enhancing the deduction to be upto Rs. 3.5 Lakhs, which, in turn would result in a benefit of around Rs. 7 lakhs over the loan period. This amendment will take effect from 1st April, 2020 and will accordingly apply in relation to assessment year 2020-21 and subsequent assessment years.

3. **Alignment of definition of “Affordable housing” as per 80-IBA with the GST Act:** Under 80-IBA of the IT Act, an assessee is allowed a 100% deduction of the profit and gains derived from the business of developing and building housing projects. The Government has taken a step to align the definition of Affordable housing with the following modifications to section 80-IBA of the IT Act:

   (i) the assessee shall be eligible for deduction under the section, in respect of a housing project if a residential unit in the housing project have carpet area not exceeding 60 square...
meter in metropolitan cities or 90 square meter in cities or towns other than metropolitan cities of Bengaluru, Chennai, Delhi National Capital Region (limited to Delhi, Noida Greater Noida, Ghaziabad, Gurgaon, Faridabad), Hyderabad, Kolkata and Mumbai (whole of Mumbai Metropolitan Region); and

(ii) the stamp duty value of such residential unit in the housing project shall not exceed forty five lakh rupees;

These amendments will take effect from 1st April, 2020 and will, accordingly, apply in relation to assessment year 2020-21 and subsequent assessment years.

The above amendment, coupled with the erstwhile reduction in GST rate on affordable housing from 8% to 1% in the 33rd GST council meeting, can be seen as a beneficial move for affordable housing finance sector.
Housing finance regulation moves to the RBI: NHB to focus on development and refinancing role

By way of implementation of something which was being discussed for a long time, the Budget 2019 has proposed amendments, whereby the regulation of housing finance companies (HFCs) will be moved from the National Housing Bank (NHB) to the RBI. Thus, the almost-100 HFCs, accounting for nearly half of the mortgage-financing in the country, will now be under the regulatory framework of the RBI.

Long-discussed proposal

NHB is currently engaged in mainly 3 functions – promotional, refinancing, and regulatory. As a promotional body, NHB acts as an instrumentality for implementation of various policies and programmes of the government concerning housing finance in the country. NHB also provides refinance to HFCs under its refinance window. Additionally, NHB is also the regulator of all HFCs. A company, which is principally engaged in housing finance, is regarded as HFC, and has to be mandatorily registered with the NHB. NHB comes up with prudential and regulatory guidelines for HFCs.

Most of the NHB regulations are at par with those of the RBI in case of NBFCs – however, there have been gaps, both in terms of time lag, and substantive differences, in many cases.

The proposal to demarcate the present three-fold functions of NHB, and let the regulatory role be transferred to the RBI, has been discussed for quite some time. In fact, the Standing Committee on Finance of the Parliament, in its 65th Report11, has discussed this issue. The Committee recommended: “The Committee note that it is proposed to confer powers relating to registration of housing finance companies to the RBI, which hitherto has been vested in the National Housing Bank”.

Statutory amendments and effective date

The Budget has proposed amendments to the NHB Act to implement the proposal. The proposals will be effective from a date to be notified, of course, after the Finance Bill is signed into a law.

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As per the scheme of the amendments, while the registration and regulatory framework of HFCs will still be governed by the NHB Act, but the regulatory powers are being conferred on the RBI.

**How does the proposal impact the state of housing finance**

Importantly, NHB will now be able to focus solely on its promotional and refinancing role. This will, potentially, enable NHB to focus more closely on the issues facing the housing finance sector, and promotional measures such as securitisation and covered bonds. The RBI, on the other hand, may focus on supervisory functions.

Housing finance companies have recently been in the news for asset liability mismatches, and consequent investor concerns. While it is difficult to say that the present regulatory set up is to share responsibility for the same, however, the new scenario should hopefully lead to better regulation.

**How does it impact HFCs**

HFCs will now have to move to the new regulator – viz., the RBI. Whether the existing regulatory step of the RBI handling NBFCs will handle HFCs as well, or a new team/division/department, will be created, remains to be seen.

Surely enough, the RBI is much stronger, has far greater strength and capabilities to carry regulatory and supervisory functions.

All existing HFCs will automatically stand registered. However, in case of any applications which are pending with the NHB for registration will now be shifted to the RBI. This will obviously result into transitional delays.

The regulatory set up for HFCs moving to the RBI does not mean the distinction between NBFCs and HFCs will get eliminated, and that all the existing regulatory statements applicable to NBFCs will become applicable to HFCs as well. In fact, HFCs will, potentially, be a separate class of financial entities. The existing definitional distinction between HFCs and NBFCs, based on principality of business, will still remain.

**How does it impact new entrants in housing finance**

As we mentioned, existing HFC applications already under process with NHB may be affected by transitional delays.

However, more importantly, will the new regulatory framework mean more new entrants in housing finance business? India currently has an ambitious target of Housing for All by 2022, and there is a huge expansion of capacity required. The existing number of HFCs needs to be

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12 There are 13 applications currently under process: [https://nhb.org.in/status-of-applications-received/](https://nhb.org.in/status-of-applications-received/)
supplemented by a large number of regional and small operators. There has been a substantial increase in the number of HFCs, but it seems more players may be required.

The RBI will, therefore, be tasked with formulation of policy towards entry in housing finance and process applications accordingly.
More regulatory powers over NBFCs

As if a suggestion of how the present state of the NBFC sector needs more regulatory powers, the Budget 2019 contains several legislative measures, aimed at giving more regulatory powers to the RBI. The backdrop of these amendments may be some of the recent episodes in the financial sector.

**Power to remove directors**

Among the proposed changes by way of Finance Bill, a new section 45I-D is to be inserted in the RBI Act, whereby the RBI will have the power to remove a director of an NBFC. There are similar powers in case of banking companies under the Banking Regulation Act.¹³

According to the proposed section, if the RBI is satisfied on any of the following grounds, it may, by order, remove any director of an NBFC. The grounds are:

a. Public interest  
b. Interest of depositors and creditors  
c. Financial security  
d. To secure proper management.

Obviously, the last item is quite wide, and will allow RBI to make a case for change of management, if it is satisfied that there has been mismanagement.

In the past, there have been instances where, in some leading NBFCs, even the role of independent directors has come for sharp scrutiny by the RBI.

An opportunity of representation will be given to the concerned director, should the RBI consider such an action.

If such an action is taken by the RBI, the concerned person will not be removed as a director of the NBFC, but will be rusticated from the boards of any other NBFC as well, for a period upto 5 years. Not only this, the concerned person shall not, in any manner, be involved in the management of an NBFC.

The RBI may, while ordering removal of a director, replace the outgoing person by a person of its choice, who shall hold office for such period as determined by the RBI.

**Administration order for an NBFC**

Section 45I-E proposed to be inserted proposes even more exceptionally serious power to the RBI – the power to supersede the Board of Directors, and appoint an administrator for a period upto 5 years. Administration

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¹³ Section 36-AA
orders are typically there in case of companies in or near insolvency, and are commonly used for bail-out. However, the proposed section does not appear to be limited to situations of distress or aimed at resolution of the NBFC. In fact, the Financial Resolution and Depositor Insurance Bill is itself a separate law and may be coming to the Parliament soon.

The grounds/circumstances in which section 45I-E can be triggered are similar to those in section 45I-D – however, since this section demolishes the whole board of directors, it is obvious that the malaise that the RBI is trying to tackle is not limited to a particular director (who can be replaced under section 45I –D): it is the entire Board which needs to be superseded.

Not only does the administration order take away the powers of the Board of Directors, even the need for any resolution of shareholders gets dispensed with. Thus, the administrator gets free hand to run the management of the NBFC.

The administrator will facilitate the reconstitution of the Board of Directors before completion of the administration orders.

In some of the cases in the recent past, the Central Govt. had to invoke powers under the Companies Act to seek appointment of directors/special officers in case of beleaguered NBFCs. The proposed section gives the power to the RBI. This fills a gap in the law.

**Barring auditors for any RBI-regulated entities**

One may try to search for motivations for this proposal, but a proposed insertion by way of section 45-MAA provides that if an auditor fails to comply with the directions of the RBI given under section 45-MA, the RBI may issue order removing and/or debarring the auditor for functioning as an auditor of any RBI-regulated entities.

Section 45-MA presently refers to the RBI’s Auditors’ Report Order, which requires auditors to report breaches of the regulatory framework in case of NBFCs to the RBI. In fact, since the present section 45-MA has very clearly delineated scope, the presently vague and seemingly very wide scope of prohibitory powers of the RBI gets delimited by the proposed insertion.

However, it may be noted that RBI-regulated entities include banks, NBFCs, asset reconstruction companies, etc.

**Powers for resolution of NBFCs**

One of the issues under the current set up is that the scope of the Insolvency and Bankruptcy Code does not cover some NBFCs. At the same time, the Financial Resolution and Deposit Insurance Bill is yet to be enacted, leaving a vacuum as far as NBFCs are concerned.
The Bill now seeks to insert a new section 45-MBA whereby the RBI will get powers to order amalgamation, splitting, and reconstruction of NBFCs. This power may be exercised by the RBI in (a) public interest; (b) interest of financial stability; or (c) continuation of activities which are critical to the financial system.

**Inspection powers and information relating to “group companies”**

As a very interesting new proposed power, the proposed section 45-NAA empowers the RBI to require the financial statements of NBFCs to contain information about “group companies”. Not content with this, the RBI also seeks to have powers to do inspection or audit of any “group companies”.

For this purpose, the term “group companies” shall include:

(i) subsidiary—parent (as may be notified by the Bank in accordance with Accounting Standards);

(ii) joint venture (as may be notified by the Bank in accordance with Accounting Standards);

(iii) associate (as may be notified by the Bank in accordance with Accounting Standards);

(iv) promoter-promotee (under the Securities and Exchange Board of India Act, 1992 or the rules or regulations made thereunder for listed companies);

(v) related party;

(vi) common brand name (that is usage of a registered brand name of an entity by another entity for business purposes); and

(vii) investment in equity shares of twenty per cent. and above in the entity;

Those familiar with the regulations will realise that the above definition is the same as has been used in context of aggregation of asset limit for computing systematic significance.

However, strangely, there are repeated references to “as may be notified by the Bank” – which would mean it will not just be sufficient for the entity to be a group entity as per the applicable accounting standards; such entity will also have to be notified by the RBI. This is both unnecessary, as well as undesirable.
Gifts galore for the NBFC sector

Non-Banking Financial Company (NBFC) have gained significant influence in the Indian economy over the past decade. In terms of credit creation, NBFCs play an equally important role as banks in India. In fact, until the first half of the FY 2019, the credit growth of NBFCs was higher than the credit growth of banks. However, the sector was hit by a liquidity crisis in second half of the year and it led to a significant drop in the credit disbursements by the NBFCs.

The liquidity crisis was due to an apprehension among the banks and mutual funds created due to failure of some leading non-banking entities in repaying their debt. The default by these ultra-large financial institutions made the banks and mutual funds wary of taking direct exposure in NBFCs. Resultantly, the liquidity of the entire sector was sucked up. So far so, that several NBFCs stopped fresh disbursements.

The figure below shows the growth of credit by loans and advances since June, 2016.

![Growth of loans and advances by NBFCs since June, 2016](image)

Source: Economic Survey, 2018-19 [Expressed in terms of percentage]

Consequent upon the unfortunate turn of events, the Reserve Bank of India formulated several directives, first for infusing liquidity into the sector and second, to strengthen the asset liability management framework for the NBFCs.

Therefore, based on the concentricity of nature of recent developments for the sector, it was expected the budget will have something similar for the
NBFCs. The author of this article has attempted to draw discuss about what the expectations were from the Budget and the actual outcome.

**Expectations**

- **Greater surveillance of NBFCs**
  
  While the regulatory bodies have become extremely cautious about the way the NBFCs have been operating lately, however, it was expected that the Budget would also have something of that sort.

- **Easy access of finance for the NBFCs**

  Ever since the ILFS episode, followed by few episodes of default by some HFCs in honouring their obligations towards Commercial Papers, banks and mutual funds became wary of taking direct exposures on them. The extra-cautious approach of the banks in extending finance to the NBFCs sucked up the liquidity from the entire segment, the figures below shows the trend of deployment of funds by mutual funds into NBFCs, banking credit to NBFCs and the growth of assets and liabilities of the NBFCs. Since, then, the industry has been struggling to breathe. It was expected that the MOF will come up with a measure to reinstate stability in the industry.
Growth rates in assets and liabilities of NBFCs
Source: Financial Stability Report, H1 FY 2020

➤ Tax parity with banks

Another expectation, which has been long awaiting, is tax parity with respect to booking of income on non-performing assets and non-payment of TDS on interest component of loans extended by them. The amendments were expected in sections 43D and 194A to allow NBFCs to take benefits of the same. Section 43D currently allows the banks to recognise income on NPAs only on realised basis, and, section 194A exempts borrowers from deducting TDS on interest payments to banks.

Actual outcome

As was expected from the Union Budget, the FM has introduced plethora of changes in the NBFC sector and several of which will have a progressive impact on the sector. The changes have been discussed below:

➤ Tax parity with banks

As may be noted above, the industry expected tax parity with banks at least for the purpose of sections 43D and 194A. The expectations were partially met by the FM as the provisions of section 43D were made applicable to deposit taking NBFCs and systemically important non deposit taking NBFCs. The non-systemically important NBFCs, however, have been kept out of the purview of the section. The section allows the certain classes of financial institutions to recognise income on non-performing assets (NPA) only on cash basis. Those not covered under the section are required to book income on NPAs on accrual basis.

➤ Greater surveillance on NBFCs

The Budget emphasised on increased surveillance on NBFCs. Necessary changes in this regard have been proposed in the RBI Act, 1934. The changes propose to provide additional powers to the RBI to remove
directors or supersede the actions of the board or carry out resolution of NBFCs in case stress etc. This issue has been dealt with in a separate chapter.

- **Fund raising by NBFCs**

  A number of measures have been taken in order to ease down the fund raising scenario for the NBFCs, the reason obviously being the ongoing liquidity stress in the sector. The proposed reforms in this regard are as follows:

  - FII and FPI investments in debt securities issued by NBFC-IDFs to be transferred/ sold to other domestic investors within the specified lock-in period.

  - Debenture redemption reserve - Withdrawal of provisions relating to debenture redemption reserve in case of bond issuances altogether. Until now, NBFCs were required to create debenture redemption reserve for publicly issued debt securities, however, privately placed debt securities were devoid of this restriction. It has now been proposed that the requirement of debenture redemption reserve be scrapped off even for publicly issued debentures. This is will certainly motivate the NBFCs to avail the bond market route for fund raising.

    The question that arises here is whether this relaxation will be applicable on the future debt issuances only or on the ongoing cases as well. The draft law in this regard is yet to be presented, therefore, this question will remain unanswered until the relevant text of the law is introduced.

  - Partial credit guarantee by the Central Government – In order to assist the NBFCs to come out of the liquidity crisis, the RBI introduced several reforms which would allow them to raise funds from the market. One of such reforms was the relaxation of the norms relating to minimum holding period of assets for the purpose of direct assignment or securitisation of such loans. This relaxation was introduced by the RBI after sensing the mood of the banking companies, which preferred acquiring asset pools originated by the NBFCs instead of taking direct exposures on them. The reason was simple – the credit quality of the assets were better than the credit quality of the NBFC. The trend has continued thereafter and now direct assignment of asset pools has become one of major sources of finance for the NBFCs.

    In order to promote such transactions further, the MoF has proposed to offer one time six months’ partial credit guarantee to public sector banks, to the extent of ₹ 1 lakh crores, for acquisition of high rate pooled assets of financially stable NBFCs. The support will be in the
nature of first loss default guarantee to the extent of 10% of the total pool size. However, specifications like – the meaning of financially stable NBFC, meaning of high rated pool etc. have not been prescribed.

This support will certainly push direct assignments volumes further, which has already been on a high since the NBFC liquidity crisis.

➢ **Change in Factoring law to allow NBFCs to participate in TReDS**

As per current framework of factoring transactions in India, that is, Factoring Regulation Act, 2011 read along with various directions issued by the RBI, in order to carry out factoring activities, an entity must be registered as an NBFC-Factor. No other company apart from an NBFC-Factor is allowed to carry on factoring. In order to encourage more participation in the TReDS, the factoring law is proposed to be amended which would allow other NBFCs to also carry out factoring activities.

In India, factoring continues to be an underutilised financing instrument and this change can lead to a substantial growth in the factoring volumes in India.

**Conclusion**

The Budget 2019-20 was full of goodies for the NBFC sector. It seems the Government has slowly started understanding the relevance of a dynamic NBFC sector in the economy. All the reforms introduced for the sector are extremely important and relevant considering the current landscape for NBFCs in India. It is expected this Budget will resolve several of the issues that the sector is currently facing.
Partial credit guarantee for banks acquiring NBFC pools: Support may have strong symbolic value

One of the proposals in the Union Budget, 2019 by the Finance Minister is a Government’s partial guarantee for public sector banks buying NBFC’s well-rated pools. The measure may have a substantial symbolic value, indicating the Government’s faith and support for what is currently a reality of the market – the bank-NBFC interface in form of direct assignments and pass-through certificates. The real stake of the Govt. in the so-called partial guarantee may not be much – given the fact that the guarantee has only a 6-month term; however, this may still encourage public sector banks to get more active in buying NBFC pools.

Banks’s investment in NBFC pools:
The sharp increase of NBFCs in the overall lending market in the country, particularly in context of small borrowers, personal finance and auto financing, has been happening in collaboration, and not competition, with banks. NBFCs have much stronger distribution abilities – they have wider geographical outreach, strong interface with borrowers, faster turn-around time, etc. On the other hand, banks are strong warehouses of money. Therefore, there is a clear case of collaboration.

The so-called collaboration is currently happening, largely, in two ways – direct assignments, and securitisation. Direct assignment is a case of transfer of proportional share in a pool, without any credit enhancements by the selling NBFC. On the other hand, securitisation is credit-enhanced, and mostly in form a security called “pass-through certificates”.

There is, now, an additional window- co-lending between the NBFC and the bank, where the NBFC becomes a minimum 20% co-lender.

Direct assignments: a great liquidity route for NBFCs
As direct bank lending dried up for NBFCs in the recent few months, direct assignments have been the way of life for NBFCs. Last financial year 2018-19 saw an over-100% spike in the volumes of securitisation, mostly in form of direct assignments.

If bank lending dries up, and the direct assignment route is not available, NBFCs will face several asset-liability mismatches, as most of them took the continuous availability of bank lending as almost assured.

Currently, NBFCs were undergoing that threat of asset-liability mismatches, hitting their ability to sustain business.
The Finance Minister’s proposal

Para 90 of the Budget Speech says:

For purchase of high-rated pooled assets of financially sound NBFCs, amounting to a total of Rupees one lakh crore during the current financial year, Government will provide one time six months’ partial credit guarantee to Public Sector Banks for first loss of up to 10%.

While the actual details may be studied only when the scheme is launched, the following features appear to be relevant:

- The scheme seems relevant in case of direct assignments, and not securitisation. In case of securitisation, the first-loss is anyways taken by the assignor, by way of subordination or other forms of credit enhancement. In case of direct assignments, as the sharing of the risks is pari passu, the need for a first loss support may arise.
- The amount of Rs 1 lac crore seems to be the pool size. As per relevant regulations, there has to be at least 10% retention by the selling NBFC. Whether the amount of Rs 1 lac crore is after considering the 10% retention, or before, remains to be seen.
- The government guarantee is only to the extent of loss taken by the acquiring bank. That would mean, the loss must be distributed pari passu between the NBFC and the bank first, and then whatever is the share of loss of the bank, will stand compensated by the first loss support given by the Govt. There is no support for the loss taken by the NBFC itself.
- Also, while one needs to see the fine print of the scheme, but the scheme may potentially provide for loss of principal invested by the bank. The question of any loss of principal arises only if the spreads are completely exhausted by the losses.
- Most importantly, the partial guarantee is only for the losses suffered by the bank for first 6 months. Generally, in case of any pools, losses are back-heavy – losses take place towards the later part of the life of a loan.
- Also, the tricky part may be – there may be a loss or shortfall in collections, but the same may get recovered later. If the performance of the defaulted loans results into recovery, the investing bank may recover its losses. Quite likely, in that case, there will be no financial stake for the Govt.

For all these reasons, the actual financial burden of losses on the exchequer will be quite small. However, as an exercise of confidence building on the NBFC sector, the proposal is sound and welcome.
SECTION-III
Starting it up
Budget 2019 is not a budget for the next eight or nine months, but has been prepared as a roadmap for the next five years of the government. The government had promised to lessen regulatory requirements for startups, besides cutting their tax compliance burden. Post the laxity in the interim budget, the startup sector was expecting more affirmative from this budget. The fintechs also had high hopes that the budget would offer special tax incentives to the sector.

Considering the fact that start-ups in India are taking firm roots and their continued growth needs to be encouraged, startups have been given a whole set of tax benefits.

**Dedicated television programme**

It has been proposed to introduce a television programme within the DD bouquet of channels exclusively for start-ups. The programme would serve as a platform for promoting start-ups, discussing issues affecting their growth, matchmaking with venture capitalists and for funding and tax planning. Further, the channel shall be designed and executed by start-ups themselves.

The startup TV is a move to praise entrepreneurship and could be a source of marketing and spreading information.

**No scrutiny from IT Department**

Angel tax is applicable to unlisted companies that have raised capital through sale of shares at a value above their fair market value. This excess capital is treated as income and taxed accordingly. The tax was first introduced in 2012 to curb money-laundering through the sale of shares of private unlisted companies at bloated prices.

It has been proposed that the 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 valuations of share premiums. This will ensure that funds raised by start-ups will not require any kind of scrutiny from the Income Tax Department. Further, a mechanism of e-verification shall be put in place to resolve the issue of establishing identity of the investor and source of his funds.

Earlier in February, the government had exempted investments of up to ₹25 crore in eligible companies from angel tax, as well as the scrutiny.

Additionally, for pending assessments of startups and redressal of their grievances, a special administrative arrangements shall be made by Central Board of Direct Taxes (CBDT). It will be ensured that no inquiry
or verification in such cases will be carried out by the Assessing Officer without obtaining approval of his supervisory officer.

**Valuation of shares**

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). The budget proposes to extend this benefit to Category-II Alternative Investment Funds also. Therefore, Valuation of shares issued to Category-II AIF shall be beyond the scope of income tax scrutiny.

**Carry forward and set off of losses**

Section 79 of the Income Tax Act, 1961 provides conditions for carry forward and set off of losses in case of a company not being a company in which the public are substantially interested.

To facilitate ease of doing business in the case of an eligible start-up, it is proposed to amend section 79 so as to provide that loss incurred in any year prior to the previous year, in the case of closely held eligible start-up, shall be allowed to be carried forward and set off against the income of the previous year on satisfaction of either of the following conditions:

1. On the last day of the previous year, the shares of the company carrying not less than fifty-one per cent of the voting power were beneficially held by persons who beneficially held shares of the company carrying not less than fifty-one per cent of the voting power on the last day of the year or years in which the loss was incurred.
2. All the shareholders of such company who held shares carrying voting power on the last day of the year or years in which the loss was incurred, continue to hold those shares on the last day of such previous year and such loss has been incurred during the period of seven years beginning from the year in which such company is incorporated.

However, for other closely held companies, no change has been proposed and loss incurred in any year prior to the previous year shall be carried forward and set off only on satisfaction of the first condition only.

**Capital Gain**

The provisions of the section 54GB of the IT Act, *inter alia*, provide for roll over benefit in respect of capital gain arising from the transfer of a long-term capital asset, being a residential property owned by the eligible assessee.
To be able to get benefit of this provision, the start-up is required to ensure the following-

1. Utilise the net consideration for subscription in the equity shares of an eligible company before the due date of filing of the return of income;
2. Have more than fifty per cent share capital or more than fifty per cent voting rights after the subscription in shares in the eligible company;
3. Not transfer assets acquired by the company for five years from the date of acquisition.

Currently the benefit of this section was only available for investment in the equity shares of eligible start-ups and that period also got over on 31st March 2019. In order to incentivise investment in eligible start-ups, the following amendments have been proposed with effect from April 1, 2020-

1. Extension of the period of exemption of capital gains arising from sale of residential house for investment in start-ups up to 31.3.2021.
2. Relaxation of the condition of minimum shareholding of fifty per cent of share capital or voting rights to twenty five per cent.
3. Relaxation of the condition restricting transfer of new asset being computer or computer software from the current five years to three years.

The budget has been favourable for the startup community. The continued attention given by the government to start-ups has been appreciated by one and all.
Micro Small and Medium Enterprises: Hits and misses under the Union Budget 2019

Introduction
MSMEs sector is a strong pillar aiding the growth of Indian economy. It contributes significantly to the economic and social development of the country by fostering entrepreneurship and generating employment opportunities. MSMEs are complementary to large industries as ancillary units and this sector contributes significantly in the inclusive industrial development of the country. Presently, the MSMEs are endeavouring to widen their domain across sectors of the economy, producing diverse range of products and services to meet demands of domestic as well as global markets.

With around 63.4 million units throughout the geographical expanse of the country, MSMEs contribute around 6.11% of the manufacturing GDP and 24.63% of the GDP from service activities as well as 33.4% of India’s manufacturing output. They have been able to provide employment to around 120 million persons and contribute around 45% of the overall exports from India. The sector has always been on focus, which is evident from the plethora of reforms proposed through the interim budget of 2019.

The expectations were similar from the incumbent government, as it came back to power once again. The author of this article has attempted to discuss about what the expectations were from the Budget and what final outcome is.

It was expected there will be reforms for the sector will revolve around the following four areas:

- Tax aspects
- Employment opportunities
- Credit availability
- Delayed payments
Tax aspects:

Background: Usually, taxation provisions are applicable to all kinds of entities in the same manner. Due to this, many times, MSMEs end up paying taxes at the same rates as paid by large entities despite the huge differences in their profits. The 2018 budget responded to this call by relaxing the income tax rate on entities having turnover upto Rs. 250 crores to 25% in place of 30% rate on corporate entities and the same was well acclaimed by this sector.

Expectations: Considering the sensitivity of the sector and also the lack of proper understanding in the segment, the MSME sector this time primarily demanded two things – a) simplification of the tax laws for them and b) specific exemptions under income tax laws. The expectations can be summarised as:

- Specific tax exemptions for MSMEs.
- Provisions with respect to applicability of indirect taxes be pegged with profits of the MSMEs instead of turnover.
- Relief from comprehensive compliance requirements under GST law.
- GST consolidation under three slabs: zero percent, five percent, and 16 percent.
- Incentive of refunding of all unrebated central and state taxes and levies on inputs used in exports of these units.

Actual: The propositions made or rather, lack of them, made in the budget with respect to tax aspects disappointed the MSME sector as only one proposition stating that entities with annual turnover upto Rs. 400 crores shall pay income tax at reduced rate of 25% instead of 30% which pretty much stays away from affecting the sector in any manner.

Employment opportunities:

Background: MSME sector generates employment for a huge chunk of masses in the country. The problem of unemployment still persists and the need of the hour calls for schemes to promote employment in the country. Schemes like skill India and MUDRA have been operative but consistently failing to address the issues of unemployment. Further, MSME sector tends to remain not-so-alluring to job seekers.

Expectations: The market expected the government to formulate more employment generation schemes specifically for MSME sector.

Actual: The budget seems to be oblivious to specific requirements of MSMEs for employment generation incentives and schemes. However, certain general policies in this regard have been proposed which are also expected to have positive impact on employment in MSME sector. Setting up of more Common Facility Centres (CFCs) is one such initiative. This is likely to facilitate cluster based development to make
the traditional industries more productive, profitable and capable for generating sustained employment opportunities. The focused sectors are Bamboo, Honey and Khadi clusters which fall under the category of rural MSMEs.

**Easy availability of credit:**

*Background:* One of the biggest challenges faced by MSMEs is lack of formal sources of capital. Various measures like 59-minute loan scheme, interest subvention scheme for MSMEs, interest relief of two percent points per annum for loans up to Rs. 1 crore etc. were earlier introduced to provide easy credit to MSMEs. Under the Interest Subvention Scheme for MSMEs, 350 crore has been allocated for FY 2019-20 for 2% interest subvention for all GST registered MSMEs, on fresh or incremental loans.

*Expectations:* The industry expected further measures making availability of funds easier for MSMEs, including:

- Access to affordable, collateral-free credit remains one of the most important areas of concern for the MSME ecosystem.
- The norms associated with banks or financial institutions giving loans towards MSME should be made simpler and quicker.
- New schemes that provide collateral free loans of up to Rs 5 million should be launched under *Pradhan Mantri Mudra Yojana*
- A scheme on the lines of Kisan credit card and providing merchant credit cards to registered merchants.

*Actual:* The budget did not come up with any new schemes for making credit easily available to MSMEs but it was stated that schemes like the Interest Subvention Scheme, 59-minute loan scheme etc. will be carried on with more zeal in the coming times.

**Delayed Payments:**

*Background:* MSMEs face a constant liquidity crunch due to delayed payments by their customers. In this regard, the Government has already taken several initiatives. Promotion of Trade Receivables Discounting System (TReDS) has been one of key initiative of Government. The Government has made it mandatory for large corporates availing supplies from MSME vendors, to mandatorily get themselves registered with TReDS so that the MSMEs can discount their invoices in the platform.

Another measure in this areas has been the introduction of disclosure requirements for companies failing pay the dues of the MSME vendors beyond 45 days. Though this is not a direct move for improving the liquidity for the segment, but since this acts as a deterrent for the large
corporates, especially the listed ones, to hold back money, this will improve the situation.

*Expectations:* Although strict requirements relating to timely payments to be made to MSMEs and measures like TReDS have been introduced, the issues of liquidity are not completely resolved. The industry expected reforms in this direction. Further measures to improve and enhance operations on TReDS platform were also expected. Also, certain recommendations from RBI regarding enhancing scope of entities that can operate on TReDS platform were expected to be considered in the union budget.

*Actual:* Seemingly, the budget intended to solve liquidity issues of MSMEs and lay strict control over customers of MSMEs. The budget stated that government will create a payment platform for MSMEs to enable filing of bills and payment thereof on the platform itself.

RBI’s recommendations on creating a second window for reverse factoring of bills of MSMEs has got cold feet after the budget failed to take it into consideration. However, the FM did propose that necessary amendments be made in the Factoring law to allow all NBFCs to participate TReDS.

**Other areas:**

Apart from the issues discussed above, other issues faced by MSMEs such as lack of ready market for their produce, burden of compliance of various laws which is at disparity with their size, lack of formalisation etc. also keep the MSMEs worried. Reforms around these were also expected. Also, incentives available for MSMEs are all-size based and are in continuation for a prolonged period. Experts believe that the benefits of an incentive can be extracted in the initial stages only.

Following are some of the reforms which were expected:

- Mandate for procurement priority from the MSMEs by PSUs.
- Special allocation for micro and small enterprises in comparison with medium scale industries.
- Some relaxation in terms of security deposits given by MSMEs to the PSU/private limited/limited/government sector.
- Measures to improve the welfare of small traders, such as establishment of National Traders’ Welfare Board, creation of a National Policy for Retail Trade etc.
- Basis for defining MSMEs to be aligned with global practices.
- Digitalisation of KYC procedures.
- Easing out of various procedural requirements relating to KYC norms, deposits etc.
- Service sector focused growth policies.
• All-size based incentives to be bound by a sunset clause of less than 10 years.

Actual: The union budget 2019 tries to address these issues by promising to provide “Protection to MSMEs”. However, no specific plans were announced in this regard.

Conclusion
The proposals made in the Budget is likely to impact the sector in the long run, however, there is hardly anything that would give the sector an instant push. It seems the MSME sector will have to keep riding on the existing policies, at least, until the next Budget.
SECTION-IV
Surveillance
Enhanced due diligence under PMLA

The provisions of Prevention of Money-Laundering Act, 2002 and the Prevention of Money-Laundering (Maintenance of Records) Rules, 2005 requires reporting entities to follow certain customer identification procedure while undertaking a transaction either by establishing an account based relationship or otherwise and monitor their transactions. The definition of reporting entities includes financial institution such as chit-fund company, housing finance institution, non-banking financial company etc.

Rule 9 of the Prevention of Money-laundering (Maintenance of Records) Rules, 2005 makes it mandatory to verify records of the identity of clients. According to the provisions, at the time of commencement of an account-based relationship or while carrying out transaction of an amount equal to or exceeding rupees fifty thousand, whether conducted as a single transaction or several transactions that appear to be connected, or any international money transfer operations, the reporting entity shall be required to identify its clients and verify their identity by comparing the copy of officially valid document with the original documents.

The budget 2019 proposes the insertion of the following section 12AA dealing with enhanced due diligence:

Section 12AA.

   (1) Every reporting entity shall, prior to the commencement of each specified transaction,
      (a) authenticate the identity of the clients undertaking such specified transaction in such manner and subject to such conditions as may be prescribed;
      (b) take additional steps to examine the ownership and financial position, including sources of funds of the client, in such manner as may be prescribed;
      (c) take additional steps as may be prescribed to record the purpose behind conducting the specified transaction and the intended nature of the relationship between the transaction parties.

   (2) Where the client fails to fulfil the conditions laid down under sub-section (1), the reporting entity shall not allow the specified transaction to be carried out.

   (3) Where any specified transaction or series of specified transactions undertaken by a client is considered suspicious or likely to involve proceeds of crime, the reporting entity shall increase the future monitoring of the business
relationship with the client, including greater scrutiny or transactions in such manner as may be prescribed.

Explanation.—For the purpose of this section, “authentication” means the process as defined under subsection (c) of section 2 of the Aadhaar (Targeted Delivery of Financial and Other Subsidies, Benefits and Services) Act, 2016.

(4) The information obtained while applying the enhanced due diligence measures under subsection (1) shall be maintained for a period of five years from the date of transaction between a client and the reporting entity.

Though the term ‘specified transaction’ has not been defined in the PML Act or Rules. However, it seems that the intention is to cover the transaction specified in Rule 9 which relates to ‘Client Due Diligence’.

Accordingly, one interpretation can be that transaction of an amount equal to or exceeding rupees fifty thousand, whether conducted as a single transaction or several transactions that appear to be connected, or any international money transfer operations will require enhanced due diligence measures.

As per the proposed amendments, the reporting entity will be required to authenticate the identity of the clients undertaking such transaction and examine the ownership and financial position, including sources of funds of the client. Further, the purpose behind conducting the transaction and the intended nature of the relationship between the transaction parties is also to be recorded. Until the aforesaid authentication is carried out, the reporting entity shall not be able to enter into such transactions.

However, to avoid any confusion, necessary clarification defining the term ‘specified transaction’ is awaited.
Capital Market Reforms

Bar on Minimum Public Shareholding (MPS) proposed to be raised from 25% to 35%

Introduction
The Finance Minister in her budget speech for the year 2019-20, has mentioned that she has already proposed SEBI to raise the current threshold of MPS in listed companies which is currently 25% to 35%. The said amendment when made effective can face huge reactions from such listed companies around the country. While the proposed changes are put up with an intent to strengthen corporate governance, it might act as a reason for some to exit the security market.

Considering the present scenario of listed companies, the said proposal may require hundreds of listed companies to undergo change in shareholding once the proposed changes are implemented.

Expected Impact of Change
Although this change is still being proposed, the implementation of the same may have the following impacts:

I. Better price discovery
When the shares come out of the hands of the promoter and fall in the hands of the public, there may be chances that the trading of the shares increase leading to better price discovery in the secondary market.

II. Increased Public Ownership
The public stake in the listed companies will shoot up to 35% leading to dilution in the promoter stake.

III. Enhanced Corporate Governance standards
The increased stake of the public in the listed companies may cause some serious problems to the promoters who have been sitting tight on their shares. Presently, getting a special resolution was comparatively easier where greater number of shares are held by promoters/ promoter group. In case of listed companies having promoter shareholding of upto 75%, special resolution could be easily be passed. However, now since
the MPS is increased to 35%, this will further raise the hurdle for corporate actions favoring the internal management or promoters.

IV. Companies might consider delisting
Many companies listed in the secondary market, who want their shares to be held by their promoters to the maximum extent possible. This not only enables better control in the company especially for decisions requiring special majority but also reaps benefits ploughing back to them. With the changes coming into force, such companies may opt for delisting rather than lose control over the company due to increase in the public stake.

V. Implementing Issues

Long-term Capital Gain Tax: Where promoter shareholding is diluted via market sale, it will result in long-term capital gain tax to be borne by the promoter selling its shares.

VI. Compliances under various Regulations

➢ Any change in shareholding of an existing shareholder holding 5% of shares in the company, due to this action, resulting in change of more than 2% of their shareholding, will trigger disclosure requirements under regulation 29 of the SEBI SAST Regulations.

➢ In case of disposal of shareholding of 5% or more in a listed entity by a listed shareholder which happens to be a promoter of the investee, the same has to be disclosed by the promoter entity as a material event in terms of SEBI LODR Regulations, 2015.

➢ Further, disclosures under regulation 7 of SEBI PIT Regulations will also get triggered in case the value of trading turnover exceeds Rs. 10 lakhs.

VII. Corporate Actions to be taken for increasing MPS

Unless specifically prescribed, applicable listed companies can opt any of the following methods to increase MPS:

- Further Public Issue
- Preferential issue of equity shares
- Market sale of shares by promoters to public, or
- Private placement of equity shares
Buyback tax extended to Listed Companies

Section 115QA of the Income-Tax Act relates to tax on distributed income to shareholders. Sub-section (1) of the said section provides that a domestic company shall be liable to pay additional income-tax at the rate of twenty per cent. on the distributed income on buy-back of shares not being shares listed on a recognised stock exchange from a shareholder. It is proposed to amend the said sub-section so as to provide that the provisions contained therein shall also apply to the buyback of shares listed on a recognised stock exchange.

It is a practice in listed companies where they utilize their profits to buy back its shares instead of distributing the same to the shareholders. The reason being higher rate of tax for distributing dividend as compared to buyback of shares. To discourage this practice, it is proposed to extend the applicability of additional tax at 20% to listed companies as well.

SEBI (ILDS) Regulations and Companies Act, 2013

It has been seen that the budget has explicitly favored the NBFCs in all its might. Adding to one of these, is the doing away with the Debenture Redemption Reserve (‘DRR”) requirement in case of public issue by NBFCs.

The current scenario required that the adequacy of DRR will be 25% of the value of outstanding debentures in case of public issue while the requirement of DRR was exempted in case of private placement.

Securities Contracts (Regulation) Act, 1956

Under section 23A - Penalty for failure to furnish information, return, etc.

The penalty under this section can also be levied where the listed entity fails to furnish information, return, etc to the SEBI. Earlier the penalty was levied if the listed entity failed to report to the stock exchange only.

SEBI Act, 1992

Under section 14 - Fund

- The General Fund constituted under the said section can be utilized for capital expenditure as per annual capital expenditure plan approved by the Board and the Central Government.
- New Insertion - Reserve Fund shall be constituted and 25% of the annual surplus shall be transferred to such Reserve Fund.
- After application towards expenses, the surplus of the General Fund to be transferred to Consolidated Fund of India.

Under section 15C - Penalty for failure to redress investors’ grievances
Penalty shall be levied under the section if the listed entity fails to redress investors' grievances when called upon to do so either in writing or by means of electronic communication.

**Under Section 15F - Penalty for failure in case of stock brokers**

Penalty for non-compliance by stock brokers extended to one crore rupees.

**New Section 15HAA inserted**

Penalty for alteration, destruction, etc., of records and failure to protect the electronic database of Board inserted.

Penalty shall not be less than one lakh rupees but which may extend to ten crore rupees or three times the amount of profits made out of such act, whichever is higher.

**Conclusion**

The Union Budget 2019-20 seems to have a mixture of proposed amendments for corporate law reforms in terms of significance. One of the crucial changes is that of increase in the MPS requirements. Owing to the cumbersome and substantial steps to be taken for compliance, a challenge awaits for the listed companies once the said amendment becomes a reality. Further, the time period allowed for complying with the changes is yet to be seen.
SECTION-V
Taxation
FM’s attempt to de-stress the distressed transactions

Insolvency and Bankruptcy Code was formulated on 28th May, 2016 and since three years, the Insolvency and Bankruptcy Board of India has been very proactive in bringing out relevant amendments to the insolvency and liquidation regulations, to remove the practical roadblocks in the implementation of the Code. Further, the Reserve Bank of India has recently issued a notification on “Prudential Framework for Resolution of Stressed Assets” on 7th June, 2019 for timely and effective resolution of stressed assets. The Economic Survey 2019-2020 has mentioned that “The ecosystem for insolvency and bankruptcy is getting systematically built out. It has already led to recovery and resolution of significant amount of distressed assets as well as palpably improved business culture.” While during the last year, the Union Budget 2018 had introduced several amendments in the tax laws, easing up the stress in acquisition/transfer of the assets of companies undergoing resolution, a lot of favourable interventions were expected from the budget, this year as well.

The Finance Minister in her budget speech, stated that the financial gains from cleaning of banking system is clearly visible since the non-performing assets were reduced by over Rs. 1 lakh crores last year, and a record recovery of Rs. 4 lakh crores could also be made possible due to the Code. Below we discuss the amendments and exemptions provided in the Income Tax Act, with respect to restructuring of loss-making business enterprises.

**Significant highlights:**

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<td>1.</td>
<td>Section 50CA of the Act pegs the value of shares of an unlisted company at a notional level (fair value) and any transaction of unquoted shares below the fair value, would be ignored for determining Clause 19 of the Bill provides for exemption to transactions undertaken by certain class of persons and subject to fulfilment of certain conditions as may be prescribed by the Board.</td>
<td>Section 50CA and Section 56, regarded as anti-abuse measures, were a roadblock in case of genuine resolution plans, wherein both the acquirer of stressed assets who bid for a price lower than the</td>
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<td>the capital gain tax and seller would have to pay the capital gains tax on the difference between the notional fair value and the original cost of acquisition subject to necessary indexation, if applicable.</td>
<td>Effective Date: This amendment will take effect from 1&lt;sup&gt;st&lt;/sup&gt; April, 2020 and will, accordingly, apply in relation to the assessment year 2020-2021 and subsequent assessment years.</td>
<td>net book value and the seller thereof are liable to pay tax on the difference between the acquisition price and the underlying book value. Determination of fair market value may not be relevant where the difference in values is due to the distressed sale, more so when such sale is approved by legal authorities. Now, a specific carve out will be made for non-applicability of such provisions for matters under IBC.</td>
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<td>2.</td>
<td>Section 56(2)(x) of the Act provides that when anything is acquired at a price lower than the fair value of such property the difference between the price paid by the acquirer and such fair value would be taxable in the acquirer’s hands as notional income. This provision is applicable to the acquisition of shares of a listed company and any discount to the ruling market price would attract tax to the acquirer.</td>
<td>Clause 21 of the Bill provides for exemption to transactions undertaken by certain class of persons and subject to fulfilment of certain conditions as may be prescribed by the Board. Effective Date: These amendments will take effect from 1&lt;sup&gt;st&lt;/sup&gt; April, 2020 and will, accordingly, apply in relation to the assessment year 2020-2021 and subsequent assessment years.</td>
<td>As many big stressed companies are listed but their acquisition price could be at significant discount to the market price, this could bring in an immediate tax burden on the acquirer, and hence, there was a need for exemption of transactions relating to transfer of shares of a listed companies under insolvency resolution plans. The Board may now exclude such cases from the applicability of the said section.</td>
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<td>3.</td>
<td>Section 79 of the Act provides that where a change in shareholding has taken place in a previous year in the case of a company, not being a company in which the public are substantially interested, no loss incurred in any year prior to the previous year shall be carried forward and set off against the income of the previous year unless on the last day of the previous year the shares of the company carrying not less than 51% (fifty-one per cent) of the voting power were beneficially held by persons who beneficially held shares of the company carrying not less than 51% (fifty-one per cent) of the voting power on the last day of the year or years in which the loss was incurred.</td>
<td>Clause 22 of the Bill provides that Section 79 shall not be applicable to a company where a change in the shareholding takes place in a previous year pursuant to a resolution plan approved by the National Company Law Tribunal under Section 242 of the Companies Act, 2013, after affording a reasonable opportunity of being heard to the jurisdictional Principal Commissioner or Commissioner.</td>
<td>Any stressed company is likely to have significant tax losses and if in the resolution plan, it is proposed to merge a stressed company with a healthy company, the availability of losses would be bound by other strict riders which would put an additional burden on the acquirer. Even if the resolution plan envisages a business sale, while the acquirer may potentially be ring fenced from several of the stressed company’s past liabilities, it would also mean the latter’s losses would not be available to the acquirer. Thus, it was imperative to make the necessary changes in tax laws. The previous Budget of 2018 exempted resolution plans under IBC from the ambit of Section 79, now the current Budget proposes to restrict the application, by excluding any transaction which are approved by NCLT under Section 242 of Companies Act.</td>
</tr>
<tr>
<td>4.</td>
<td>Section 115JB of the Act provides for levy of tax on certain companies on the</td>
<td>Clause 34 of the Bill provides that the aggregate amount of unabsorbed</td>
<td>Haircut of financial and operational debts is the foundation of any</td>
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<td>Clause 34 of the Bill provides that the aggregate amount of unabsorbed</td>
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<td>basis of book profit which is determined after making certain adjustments to the net profit disclosed in the profit and loss account prepared in accordance with the provisions of the Companies Act, 2013.</td>
<td>depreciation and loss brought forward shall be allowed to be reduced from the book profit in case of a company, and its subsidiary and the subsidiary of such subsidiary, where the National Company Law Tribunal, on an application moved by the Central Government, under Section 241 of the Companies Act, 2013, has suspended the Board of Directors of such company and has appointed new directors nominated by the Central Government, under Section 242.</td>
<td>resolution plan. The taxability on waiver of loans has always been a highly controversial issue. Taxing financially stressed companies on the “notional” profit arising on loan waiver creates huge negative financial impact and liquidity issues. Therefore, there was a need for exemption for stressed entities or those undergoing proceedings under IBC.</td>
</tr>
</tbody>
</table>

Effective Date: This amendment will take effect from 1st April, 2020 and will, accordingly, apply in relation to the assessment year 2020-21 and subsequent assessment years.

Overall it appears that the approach of the Budget is positive. The Ministry has tried to align the tax provisions with the insolvency laws and also eased up the liability on the tax payers by providing for reliefs on transactions approved by National Company Law Tribunal, which will enable improvement of the economy and revival of failing business entities.
Direct tax amendments proposed under Finance Bill, 2019

Changes in Rates of taxes:
- Income tax slab to remain as applicable to AY 2019-20
- Rebate of 87A to be allowed at lower of 100% of income tax or Rs. 12,500 to resident individual with total income not exceeding Rs. 5,00,000.
- Surcharge on Individuals

<table>
<thead>
<tr>
<th>Total Income</th>
<th>Rate of Surcharge</th>
<th>Applicability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total income exceeding fifty lakh rupees but not</td>
<td>10% of income tax</td>
<td>AY 2019-20, AY 2020-</td>
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<tr>
<td>exceeding one crore rupees</td>
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<td>21</td>
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<tr>
<td>Total income exceeding one crore</td>
<td>15% of income tax</td>
<td>AY 2019-20</td>
</tr>
<tr>
<td>Total income exceeding one crore rupees but not</td>
<td>15% of income tax</td>
<td>AY 2020-21</td>
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<tr>
<td>exceeding two crore rupees</td>
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</tr>
<tr>
<td>Total income exceeding two crore rupees but not</td>
<td>25% of income tax</td>
<td>AY 2020-21</td>
</tr>
<tr>
<td>exceeding five crore rupees</td>
<td></td>
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<tr>
<td>Total income exceeding five crore rupees</td>
<td>37% of income tax</td>
<td>AY 2020-21</td>
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</table>

Steps taken by the Government to discourage cash transactions

Section 194N: TDS on cash withdrawal
(Newly inserted)

In order to make India a cashless economy, it is proposed to insert a new Section 194N where,
- TDS @2 % shall be deducted on cash withdrawals exceeding ₹ 1crore in aggregate during the year
- Person liable to deduct TDS
  - a banking company to which the Banking Regulation Act, 1949 applies (including any bank or banking institution referred to in section 51 of that Act);
o a co-operative society engaged in carrying on the business of banking; or
o a post office

- TDS shall be deducted on any person who withdraws cash exceeding ₹ 1 crore in aggregate
- This section will not be applicable to:
  o the Government
  o banking Company or Co-operative society engaged in the business of banking or post office
  o business correspondent of a banking company or cooperative society
  o any white label automated teller machine operator of a banking company or co-operative society
  o such other person or class of persons, which the Central Government may, by notification in the Official Gazette, specify in consultation with the Reserve Bank of India

*The proposed section shall be effective from 1st September, 2019*

**Section 269SU: Mandating acceptance of payments through prescribed electronic modes**

*(Newly inserted)*

- This section is applicable on every person carrying business who’s total sales, turnover, gross receipts exceeds ₹ 50 crores in the preceding financial year
- Such person shall provide facility for accepting payment through prescribed electronic form.

It is also proposed to make a consequential amendment in the Payment and Settlement Systems Act, 2007 so as to provide that no bank or system provider shall impose any charge upon anyone, either directly or indirectly, for using the modes of electronic payment prescribed under section 269SU of the Income-tax Act

*The proposed section shall be effective from 1st November, 2019*

**Section 271BD: Penalty for failure to comply with provisions of section 269SU**

- Failure to comply with provisions of section 269SU attracts penalty
- A penalty of ₹ 5,000 every day during which such failure continues
- Such penalty shall be waived if there is a good and sufficient reason for such failure
- The penalty shall be imposed by the Joint Commissioner
The proposed section shall be effective from 1st November, 2019

Prescription of electronic mode of section
(Amendment)

In order to encourage other electronic modes of payment, it is proposed to amend the above sections so as to include such other electronic mode as may be prescribed, in addition to the already existing permissible modes of payment/receipt in the form of an account payee cheque or an account payee bank draft or the electronic clearing system through a bank account.

The words “bank account”, the words “bank account or through such other electronic mode as may be prescribed” shall be substituted for the following sections:

- Section 13A: Special provisions relating to incomes of political parties
- Section 35AD: Deduction in respect of expenditure on specified business
- Section 43: Definitions of certain terms relevant to income from profits and gains of business or profession.
- Section 43CA: Special provision for full value of consideration for transfer of assets other than capital assets in certain cases.
- Section 44AD: Special provision for computing profits and gains of business on presumptive basis.
- Section 50C: Special provision for full value of consideration in certain cases.
- Section 56: Income from other sources
- Section 80J/JAA: Deduction in respect of employment of new employees

The proposed amendment shall be effective from 1st April, 2020

- Section 269SS: Mode of taking or accepting certain loans, deposits and specified sum
- Section 269ST: Mode of undertaking transactions
- Section 269T: Mode of repayment of certain loan or deposits

The proposed amendment shall be effective from 1st September, 2019.

Widening and deepening of tax base

Section 194-IA Payment on transfer of certain immovable property other than agricultural land.
(Amendment)
(Insertion in explanation clause for the word “consideration for immovable property” under section 194-IA, TDS at the time of purchase of immovable property)

- Section 194-IA relates to payment on transfer of certain immovable property other than agricultural land and provides levy of TDS @ 1% on the amount of consideration paid or credited for transfer of the immovable property.
- The term “consideration for immovable property” was not defined earlier.
- **Insertion in explanation clause:** “consideration for immovable property” shall include all charges of the nature of club membership fee, car parking fee, electricity or water facility fee, maintenance fee, advance fee or any other charges of similar nature, which are incidental to transfer of the immovable property;

The proposed insertion shall be effective from 1st September, 2019.

**Section 194M: Payment of certain sums by certain individuals or Hindu undivided family**

(Newly inserted)

- TDS shall be deducted @5% on the sum or the aggregate of sums paid or credited in a year on account of contractual work or professional fees.
- This section shall be applicable to individuals and HUF, not required to deduct tax at source under section 194C and 194J of the IT Act.
- This section shall not be applicable where the aggregate of sums, credited or paid to a resident during a financial year does not exceed ₹ 50 lakhs.
- Also, to reduce the burden of individuals and HUF, they may deduct tax using their Permanent Account Number (PAN) and not require to obtain Tax deduction Account Number (TAN).

The proposed section shall be effective from 1st September, 2019.

**Section 9: Income deemed to accrue or arise in India.**

(Amendment)

- Relates to Income deemed to accrue or arise in India. Under the Act, non-residents are taxable in India in respect of income that accrues or arises in India or is received in India or is deemed to accrue or arise in India or is deemed to be received in India.
- Under the existing provisions of the Act, a gift of money or property is taxed in the hands of donee, except for certain
exemptions provided in clause (x) of sub-section (2) of section 56.

- Earlier gifts made by persons being residents in India to persons outside India and are claimed to be non-taxable in India as the income does not accrue or arise in India.

- To ensure that such gifts made by residents to persons outside India are subject to tax, it is proposed to provide that income of the nature referred to in sub-clause (xviia) of clause (24) of section 2, arising from any sum of money paid, or any property situate in India transferred, on or after 5th July, 2019 by a person resident in India to a person outside India shall be deemed to accrue or arise in India.

- However, the existing provision for exempting gifts as provided in proviso to clause (x) of sub-section (2) of section 56 will continue to apply for such gifts deemed to accrue or arise in India.

- In a treaty situation, the relevant article of applicable DTAA shall continue to apply for such gifts as well.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

Mandatory furnishing of return of income by certain persons
Section 139: Return of income
(Amendment)

- Currently a person other than a company or a firm is required to furnish the return of income only if his total income exceeds the maximum amount not chargeable to tax.

- In order to ensure that high value transactions are reported for those who person whose income is not taxable, government has made it mandatory to file return by amending section 139 accordingly.

- A person shall be mandatorily required to file his return of income if during the previous year he
  - has deposited an amount or aggregate of the amounts exceeding one crore rupees in one or more current account maintained with a banking company or a co-operative bank; or
  - has incurred expenditure of an amount or aggregate of the amounts exceeding two lakh rupees for himself or any other person for travel to a foreign country; or
has incurred expenditure of an amount or aggregate of the amounts exceeding one lakh rupees towards consumption of electricity; or

- fulfils such other prescribed conditions, as may be prescribed

- Further, currently, a person claiming rollover benefit of exemption from capital gains tax on investment in specified assets like house, bonds etc., is not required to furnish a return of income, if after claim of such rollover benefits, his total income is not more than the maximum amount not chargeable to tax.

- In order to make furnishing of return compulsory for such persons, it is proposed to amend the sixth proviso to section 139 of the Act to provide that a person who is claiming such rollover benefits on investment in a house or a bond or other assets, under sections 54, 54B, 54D, 54EC, 54F, 54G, 54GA and 54GB of the Act, shall necessarily be required to furnish a return, if before claim of the rollover benefits, his total income is more than the maximum amount not chargeable to tax.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

Inter-changeability of PAN & Aadhaar and mandatory quoting in prescribed transactions.

Section 139A: Permanent Account Number

(Amendment+ New insertion)

- To ensure audit trail of high value of transactions, where the person does not possess PAN,

- Also, to ensure ease of compliance, it is also proposed to provide for inter-changeability of PAN with the Aadhaar number.

- A new sub-section (6A) is also proposed to be inserted to ensure quoting of PAN or Aadhaar number for entering into prescribed transactions and authentication thereof in the prescribed manner.

- Duty is also proposed to be cast upon the person receiving any document relating to such transactions, through newly proposed sub-section (6B), to ensure that PAN or Aadhaar number, as the case may be, is duly quoted, and authenticated.

- In order to ensure proper compliance of the provisions relating to quoting and authentication of PAN or Aadhaar, the penalty provision contained in section 272B is proposed to be amended suitably.
The proposed amendment shall be effective from 1st September, 2019.

Consequence of not linking PAN with Aadhar
Section 139AA: Quotating of Aadhaar number
(Amendment)

- The existing proviso to the sub-section (2) of section 139AA, provides that the PAN allotted to a person shall be deemed to be invalid, in case the person fails to intimate the Aadhaar number, on or before the notified date.
- In order to protect validity of transactions previously carried out through such PAN, it is proposed to amend the said proviso so as to provide that if a person fails to intimate the Aadhaar number, the PAN allotted to such person shall be made inoperative in the prescribed manner.

The proposed amendment shall be effective from 1st September, 2019.

Tax Incentives
Incentives to International Financial Services Centre (IFSC)
Section 47: Transactions not regarded as transfer
(Amendment)

In order to promote the development of world class financial infrastructure in India, some tax concessions have already been provided in respect of business carried on from an IFSC. To further promote such development and bring these IFSC at par with similar IFSC in other countries, following additional benefits are proposed:

- Under the present provisions of section 47 of the act, any transfer of a capital asset, being bonds or Global Depository Receipts or rupee denominated bond of an Indian company or derivative, made by a non-resident through a recognised stock exchange located in any IFSC and where the consideration for such transaction is paid or payable in foreign currency shall not be regarded as transfer.
- With a view to provide tax-neutral transfer of certain securities by Category III Alternative Investment Fund (AIF) in IFSC, it is proposed to amend the said section so as to provide that any transfer of a capital asset, specified in the said clause by such AIF, of which all the unit holders are non-resident, are not regarded as transfer subject to fulfilment of specified conditions.
- It is also proposed to widen the types of securities listed in said clause by empowering the Central Government to notify other securities for the purposes of this clause.
This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

**Section 10: Incomes not included in total income**  
(Amendment)

- The amendment is to promote external borrowings by units located in IFSC
- Any income by way of interest payable to a non-resident by a unit located in IFSC in respect of monies borrowed by it on or after 1st day of September, 2019, shall be exempt.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

**Section 115-O: Tax on distributed profits of domestic companies**  
(Amendment)

- To facilitate distribution of dividend by companies operating in IFSC, it is proposed to amend the provision of the said section to provide that any dividend paid out of accumulated income derived from operations in IFSC, after 1st April 2017 shall also not be liable for tax on distributed profits.

This amendment shall be effective from 1st September, 2019.

**Section 115-R: Tax on distributed income to unit holders**  
(Amendment)

- In the existing provisions of the section 115R of the Act, any amount of income distributed by the specified company or a Mutual Fund to its unit holders shall be chargeable to tax and such specified company or Mutual Fund shall be liable to pay additional income-tax on such distributed income.
- In order to incentivize relocation of Mutual Fund in IFSC, it is proposed to amend the said section so as to provide that no additional income-tax shall be chargeable in respect of any amount of income distributed, on or after the 1st day of September, 2019, by a Mutual Fund of which all the unit holders are non-residents and which fulfils certain other specified conditions.

This amendment shall be effective from 1st September, 2019.

**Section 80LA: Deductions in respect of certain incomes of Offshore Banking Units and International Financial Services Centre**
Earlier section 80LA provides profit linked deduction of an amount equal to 100% of income for the 1st five consecutive years and 50% for the next five consecutive years to units of an IFSC.

It is now proposed to provide incentive to the units in IFSC, 100% deduction shall be five for ten consecutive years.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

Section 43D: Special provision in case of income of public financial institutions, public companies, etc (Amendment)

As per matching principle in taxation, it is proposed to amend section 43B of the Act to provide that any sum payable by the assessee as interest on any loan or advances from a deposit-taking NBFCs and systemically important non deposit-taking NBFCs shall be allowed as deduction if it is actually paid on or before the due date of furnishing the return of income of the relevant previous year.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

Tax incentive for electric vehicles

Section 80EEB: Deduction in respect of purchase of electric vehicle (Newly inserted)

- Interest payable on loan for purchase of electric vehicle from any financial institution shall be liable for deduction upto ₹ 1,50,000
- the loan has been sanctioned by a financial institution including a non-banking financial company during the period beginning on the 1st April, 2019 to 31st March, 2023
- the assessee does not own any other electric vehicle on the date of sanction of loan

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.
Exemption of interest income of a non-resident arising from borrowings by way of issue of Rupee Denominated Bonds
Section 194LC: Income by way of interest from Indian company
(Amendment)

In order to incentivise low cost foreign borrowings through Off-shore Rupee Denominated Bond, the press release dated 17th September, 2018, inter alia, announced that interest payable by an Indian company or a business trust to a non-resident, including a foreign company, in respect of rupee denominated bond issued outside India during the period from September 17, 2018 to March 31, 2019 shall be exempt from tax. Consequently, no tax was required to be deducted on the payment of interest in respect of the said bond.

The exemption announced through the said press release is proposed to be incorporated in the law by amending section 10 of the Act so as to provide exemption to income payable by way of interest to a non-resident by the specified company in respect of monies borrowed from a source outside India by way of issue of rupee denominated bond, as referred to in section 194LC, during the period beginning from the 17th day of September, 2018 and ending on the 31st day of March, 2019.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

Tax benefits on Affordable housing sector

Section 80EEA: Deduction in respect of interest on loan taken for certain house property
(Newly inserted)

Deduction of maximum ₹ 1, 50, 000 on the interest payable on loan taken from a financial institution. Only applicable on loan sanctioned during period 1st April 2019 till 31st March, 2020. The stamp duty value of residential house property not to exceed forty-five lakh rupees and the assessee shall not be owning any residential house property on the date of sanction of loan.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.
Section 80-IBA: Deductions in respect of profits and gains from housing projects
(Amendment)

- Extension of the deduction to residential unit in housing projects with a carpet area not exceeding 60 sq meters in metropolitan cities and 90 sq. meters in other than metropolitan cities. (in place of erstwhile carpet area limit of not exceeding 30 sq meters in metropolitan cities and 60 sq. meters in other than metropolitan cities).
- Stamp duty value on such residential unit in the housing project not to exceed forty five lakh rupees.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

Relaxation in conditions of special taxation regime of offshore funds

Section 9A: Certain activities not to constitute business connection in India
(Amendment)

- On receipt of representations from various stakeholders, relaxation of certain conditions in the implementation of regime of fund managers are proposed.
- Following constraints proposed to be removed:
  - Corpus of the fund shall not be less than one hundred crore rupees at the end of a period of six months from the end of the month of its establishment or incorporation or at the end of such previous year, whichever is later; and
  - the remuneration paid by the fund to an eligible fund manager in respect of fund management activity undertaken by him on its behalf is not less than the amount calculated in such manner as may be prescribed.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

Incentive for start-ups

Section 79: Carry forward and set off of losses in case of certain companies
(Amendment)
• Section 79 of the Income Tax Act, 1961 provides conditions for carry forward and set off of losses in case of a company not being a company in which the public are substantially interested.
• To facilitate ease of doing business in the case of an eligible start-up, it is proposed to amend section 79 so as to provide that loss incurred in any year prior to the previous year, in the case of closely held eligible start-up, shall be allowed to be carried forward and set off against the income of the previous year on satisfaction of either of the following conditions:

1. On the last day of the previous year, the shares of the company carrying not less than fifty-one per cent of the voting power were beneficially held by persons who beneficially held shares of the company carrying not less than fifty-one per cent of the voting power on the last day of the year or years in which the loss was incurred.

2. All the shareholders of such company who held shares carrying voting power on the last day of the year or years in which the loss was incurred, continue to hold those shares on the last day of such previous year and such loss has been incurred during the period of seven years beginning from the year in which such company is incorporated.

However, for other closely held companies, no change has been proposed and loss incurred in any year prior to the previous year shall be carried forward and set off only on satisfaction of the first condition only.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

Section 54GB: Capital gain on transfer of residential property not to be charged in certain cases (Amendment)

• The provisions of the section 54GB of the IT Act, inter alia, provide for roll over benefit in respect of capital gain arising from the transfer of a long-term capital asset, being a residential property owned by the eligible assessee.
• To be able to get benefit of this provision, the assessee is required to ensure the following:

  1. Utilise the net consideration for subscription in the equity shares of an eligible company before the due date of filing of the return of income.
  2. Have more than fifty per cent share capital or more than fifty per cent voting rights after the subscription in shares in the eligible company.
3. Not transfer assets acquired by the company for five years from the date of acquisition.

- Currently the benefit of this section was only available for investment in the equity shares of eligible start-ups and that period also got over on 31st March 2019. *In order to incentivise investment in eligible start-ups, the following amendments have been proposed with effect from April 1, 2020.*
- Extension of the period of exemption of capital gains arising from sale of residential house for investment in start-ups up to 31.3.2021
- Relaxation of the condition of minimum shareholding of fifty per cent of share capital or voting rights to twenty five per cent
- Relaxation of the condition restricting transfer of new asset being computer or computer software from the current five years to three years.

*This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.*

**Incentives for Category II Alternative Investment Fund (AIF)**

- Exemption from this provision has been provided for the consideration for issue of shares received by a venture capital undertaking from a venture capital company or a venture capital fund or by a company from a class or classes of persons as may be notified by the Central Government in this behalf.
- Currently the benefit of exemption is available to Category I AIF.
- With a view to facilitate venture capital undertakings to receive funds from Category II AIF, it is proposed to amend the said section to extend this exemption to fund received by venture capital undertakings from Category II AIF as well

*This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.*

**Concessional rate of Short-term Capital Gains (STCG) tax to certain equity-oriented fund of funds**

Section111A: Tax on short-term capital gains in certain cases

- In order to further incentivise these funds of funds, it is proposed to amend section 111A so as to extend the concessional rate of
tax for short-term capital gains in respect of transfer of units of such fund of funds

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

Facilitating resolution of distressed companies

Measures for resolution of distressed companies

- The existing provisions of section 79 are not applicable to a company where any change in shareholding takes place in a previous year pursuant to a resolution plan approved under the Insolvency and Bankruptcy Code, 2016 (IBC) subject to the condition that jurisdictional Principal Commissioner or Commissioner is provided a reasonable opportunity of being heard.
- Thus, loss in such cases can be carried forward and set off even if there is change in voting power or shareholding. This benefit is proposed to be extended to certain companies.
- Thus it has been provided in newly substituted section 79 that the provision of this section shall not apply to those companies, and their subsidiary and the subsidiary of such subsidiary, where board of directors have been suspended by National Company law Tribunal (NCLT) and new Directors have been appointed by NCLT on the recommendation of the Central Government.
- It is proposed that the conditions of continuity of shareholding for carry forward and set off of losses shall not apply to such companies. Further, under section 115JB of the Act, for calculating book profit, it is proposed to provide that for the purposes of computation of Minimum Alternate Tax (MAT) liability of such companies, the aggregate of brought forward losses and unabsorbed depreciation shall also be allowed as deduction.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

Prescription of exemption from deeming of fair market value of shares for certain transactions

Section 56: Income from other sources

(Amendment)
For determining the amount of income for receipt of certain shares, the fair market value of the shares is taken into account. Section 50CA provides for deeming of fair market value of unquoted shares for computing the capital gains from the transfer of such shares. For both these provisions, the fair market value is determined based on the prescribed method. Currently, the provisions of section 56(2)(x) are not applicable to certain specified transactions. However, no such exemption is available under section 50CA. It is proposed to amend these sections to empower the Board to prescribe transactions undertaken by certain class of persons to which the provisions of section 56(2)(x) and 50CA shall not be applicable.

This amendment shall be effective from 1st April, 2020 and, accordingly apply in relation to the assessment year 2020-21 and subsequent assessment years.

Strengthening anti-abuse measures

Section 115QA: Tax on distributed income to shareholder (Amendment)

- Sub-section (1) of the said section provides that a domestic company shall be liable to pay additional income-tax at the rate of 20% on the distributed income on buy-back of shares not being shares listed on a recognised stock exchange from a shareholder.
- It is proposed to amend the said sub-section so as to provide that the provisions contained therein shall also apply to the buyback of shares listed on a recognised stock exchange.
- The amendment is in order to curb tax avoidance practice adopted by the listed companies, whereby the listed companies are also indulging in such practice of resorting to buy-back of shares, instead of payment of dividends.

This amendment shall be effective from 5th July, 2020

Removing difficulties faced by tax payers

Clarification regarding definition of the “accounting year” in section 286 of the Act

Section 286: Furnishing of report in respect of international group. (Amendment)
• It is proposed to suitably amend section 286 so as to provide that the accounting year in case of the ARE of an international group, the parent entity of which is not resident in India, the reporting accounting year shall be the one applicable to such parent entity.

• This amendment is clarificatory in nature.

The amendment will take effect retrospectively from the 1st April, 2017 and will, accordingly, apply in relation to the assessment year 2017-18 and subsequent assessment years.

Facilitating demerger of Ind-AS compliant companies

• Ind AS compliant companies are required to record the property and the liabilities of the undertaking at a value different from the book value of the demerged company.

• It is proposed to amend section 2 of IT Act to bring in alignment with the requirement of Ind AS, of recording the property and liability at a value different from the book value.

Rationalisation of provisions

Compliance with the notification of exemption issued under section 56(2)(viib)

Section 56: Income from other sources

(Amendment)

• The provisions of section 56(2) (viib) of the Act provides for charging of the consideration received for issue of shares by certain companies, where such consideration exceeds the fair market value of such shares under the head Income from Other Sources.

• Various notifications were issued by the Central Government to provide exemptions from this section subject to compliance of certain conditions.

• It is proposed to provide, with effect from 1st April 2020, that in case of failure to comply with the conditions, the consideration received for issue of shares, which exceeds the face value of such shares shall be deemed to be the income of the company chargeable to income-tax for the previous year in which the failure to comply with any of the said conditions has taken place.

These amendments will take effect from 1st April, 2020 and will, accordingly, apply in relation to the assessment year 2020-21 and subsequent assessment years.

Consequential amendment to section 56
No consequential amendment is made in section 56. It is proposed to amend section 56 of the Act to provide the correct reference of section 145B(1) in section 56, in place of the existing reference of section 145A(b).

This amendment will take retrospective effect from 1st April, 2017 and will accordingly apply in relation to assessment year 2017-18 and subsequent assessment years.

Rationalisations of provisions relating to maintenance, keeping and furnishing of information and documents by certain persons

Section 92D: Maintenance and keeping of information and document by persons entering into an international transaction or specified domestic transaction.

Section 92D of the Act requires every person who has entered into an international transaction or specified domestic transaction to keep and maintain prescribed information and document in respect thereof. It is proposed to substitute section 92D, in order to provide that the information and document to be kept and maintained by a constituent entity of an international group, and filing of required form, shall be applicable even when there is no international transaction undertaken by such constituent entity.

Improving effectiveness of tax administration

Online filing of application seeking determination of tax to be deducted at source on payment to non-residents

Section 195: Others sum

(Amendment)

- Under sub-section (2) of section 195 of the Act, an application has to be made to the assessing officer to determine the appropriate proportion of such sum chargeable in a situation where a person who is liable to make payment to a non-resident which is income chargeable to tax under the act, feels otherwise, has to obtain certificate/order from the Assessing Officer for lower or nil withholding-tax. This follows a manual process currently.
- Amendments are proposed to be made in the section in terms of the form and manner of application to the Assessing Officer and
also for the manner of determination of appropriate portion of sum chargeable to tax by the Assessing Officer.

Similar amendment is also proposed to be made in sub-section (7) of section 195 which are applicable to specified class of persons or cases. These amendments will take effect from 1st November, 2019.
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