NaMo led Budget for Markets

by CA Niyati Hemani

Savings

Increase in Personal Tax Exemption Limit, Tax Saving Investment Exemption Limit, Deduction of Interest on housing loan of a self occupied property shall all result in incremental cash flows in the hands of investor and is positive for the financial sector.

Sectoral Impact

Power and Infra are clearly two focus areas since the sunset clause for power units are extended as also support is provided to Infrastructure lending along with infrastructure development. Positive for Banking sector with measures like capitalisation of PSU Banks. Insurance sector shall get a boost as FDI limit in the same has been relaxed. Entrepreneurs and manufacturing industry are encouraged by providing deduction of investment allowance.

FII

Measures like relaxation on FDI limits, tax incentives including lower withholding tax for all types of bond investments by foreign investors, pass-through status on REITs, Infrastructure investment trust, clarity on sale of securities by FII to be treated as capital gains have augured well the confidence of FII in the Indian market.

Acche Din Aayenge !?

The maiden budget from the NaMo led government placed before the parliament on 10 July 2014 was most sought after by the people of India to DISCOVER the CHANGE and EMBARK on RAYS OF ACHHE DIN. Hopes and expectations were attached from the HIGHLY MANDATED and DEVELOPMENT ORIENTED NaMo led government. However, considering high fiscal deficits, GDP of less than 5% in past two years, rising inflation, uncertainties of the global economy and with only 45 days on hand, less could be managed in the realm of fiscal manoeuvrability.

Yet clearly skill development, e-governance, leveraging technology for social infrastructure (education and healthcare), reviving traditional industries and encouraging entrepreneurship were the MANTRAS for the NEW GROWTH MODEL. Investment plans for ports, airports, roads, agri-infra, railways, energy, defense, urbanisation and smart cities, water transport etc. were talked about.

Taxation

Duration and Taxability of Long Term Capital Asset -

Unlisted securities and mutual funds, other than equity oriented mutual funds shall qualify as 'long term capital asset', if held for more than 36 months (earlier limit: 12 months). This move is to bring parity with bank and other debt instruments.

Further, tax rate on sale of long term listed mutual funds (other than equity-oriented mutual funds) is proposed to be taxed at a flat rate of 20%. Earlier, such unlisted securities were taxable at the rate of 10% without indexation or at 20% with indexation whichever is lower.

Proposed to calculate Dividend Distribution Tax on 'gross' basis instead of 'net' basis.

DDT under section **115-O** - Increased from @16.995% to 19.9941% of dividend amount distributed

DDT under section **115-R** - Income distribution on equity oriented funds: Nil

Income distributed by Mutual Fund to an Individual/ HUF: Increased from 28.325% to 37.7667% and that of any other person: Increased from 33.99% to 48.557%

In this article, I have tried to analyze the impact of some of the provisions of the union budget 2014 keeping in mind the investor community so as to say the AAM ADAMI

A. Tax Savings

• Personal income tax basic exemption limit raised to Rs.2.5 lacs from Rs.2 lacs for general category of individuals. For senior citizens basic exemption limit raised to Rs.3 lacs from Rs. 2.5 lacs.

• Sec 80 C deduction limit increased to Rs.1.5 lacs from Rs.1 lacs.

• Interest on housing loan deduction increased from Rs. 1.5 lacs to Rs. 2 lacs in case of self-occupied property

B. Investment Savings

• Reintroduction of Kisan Vikas Patra, a bond like instrument in which the invested money doubles in a given period. It shall channelise unbanked money.

• A small saving scheme named after the girl child to cater to the requirements of education and marriage of girls.

• Relaunching of Varishta Pension Bima Yojana for senior citizens of over 60 years starting August 15.

• Employee Provident Fund and Pension scheme - The mandatory wage ceiling for PF contribution increased from monthly pay of Rs.6,500/- to Rs.15,000/. Also, employees covered under Employees Pension scheme will receive a minimum monthly pension of Rs.1,000/-.

• The investment limit for PPF has also been raised from Rs. 1 lac to Rs. 1.5 lacs allowing investors to claim tax free interest and claim benefit under section 80C as above.

• In the light of the long term capital gains tenure now extended to 3 years, investors could find favour with long duration bond and guilt funds. Preferences could be more for accrual funds as they have higher portfolio yield to maturity.

• While FIIs continue to pour money and that domestic economic revival is underway and the valuations are also reasonable, Equity market is likely to pick up.

Sr.	Market Impact
1	MFs fear outflows, AMFI has asked regulator SEBI to defer long term capital gains tax on debt oriented MFs to next financial year.
2	AMFI has also taken up the matter with the Ministry of Finance, "To have the long-term capital gain tax on closed ended debt schemes and not on open ended debt schemes, gold exchange traded funds and funds of funds etc, as this would render this asset class unattractive for investment. This in turn could impact the liquidity and development of corporate bonds."
3	Big corporates are now leaning on the finance ministry to make the changes effective from a prospective date and provide grandfathering element for the existing investors
4	Fixed Maturity Plans (FMP) and short-term bond funds are expected to be hit due to change. Switch of funds from debt funds to bank deposits is likely as the latter will have similar tax treatment.
5	A report by The Economic Times states that at least four fund houses have deferred their FMPs and two have even returned cash collected from investors for issues that closed last week.

MFs exposure to bank stocks hits record-high of Rs 55k cr. This was also the fifth consecutive monthly rise. After banking, software is the second most preferred sector with MFs having exposure followed by pharmaceuticals and Finance. Market valuation at this point in time looks fairly valued.

RBI and the government are trying to tackle to get the long-term funding market better for the infrastructure projects. However, given the weak monsoon and its impact on inflation, it is unlikely for the RBI to give support in form of interest rate easing soon

Real estate experts have given the budget a big thumbs-up as it focuses evenly on housing and development with both domestic and foreign investments in the sector. The development of smart cities can bring opportunities for real estate developers, investors, end users and the housing loan sector. Introduction of real REITS is a welcome move as it is likely to increase liquidity in the cash strapped sector. With Slum development being made a part of CSR activities, the government seems to have its heart in the right place.

Infrastructure bottlenecks continue to remain critical for the farm sector. Efforts for 2nd green revolution, setting aside funds for climate change and irrigation, introducing Kisan TV for effective dissemination of knowledge - all these would ensure a long term positive impact on farm productivity for farmers.

C. Certain Direct Tax Burdens

- **Deduction of tax at source from payment in respect of life insurance policy**

With effect from 1 October 2014, tax to be withheld at the rate of 2 per cent at the time of payment on sum paid under a life insurance policy, including the sum allocated by way of bonus, which are not exempt. It has also been proposed that no deduction of tax under this provision shall be made if the aggregate sum paid in a financial year to an assessee is less than INR 1,00,000.

- **Capital gain on transfer of certain capital assets not to be charged in case of investment in only one residential house**

This amendment clarifies that 'a'residential house has now to be restricted to 'only one residential house situated in India'.

- **Capital gain not to be charged on investment in certain bonds made in the financial year**

The existing provision states that the investment made in the long-term specified asset during any financial year shall not exceed fifty lakh rupees. The amendment clarifies that the tax exemption will be limited to Rs. 50 lakhs even where re-investment in certain bonds is split between two different financial years.

- **Transfer Pricing - Definition of deemed international transaction expanded**

Amendment seeks to broaden the scope of a deemed international transaction. The deeming fiction would continue to apply irrespective of whether the non-associated enterprise is a resident or not. Hence the deeming fiction would now also extend to transactions between two resident enterprises.

- **Non-Deductibility of the CSR Expenditure**

As the CSR expenditure, being an application of income, is not incurred for the purposes of carrying on business, such expenditures cannot be allowed under the existing provisions of section 37 of the Income-tax Act. However, the CSR expenditure which is of the nature described in section 30 to section 36 of the Income-taxAct shall be allowed as deduction under those sections subject to fulfilment of conditions, if any, specified therein.

D. Towards Direct Tax Certainty

- **Speculative Transaction**

It is proposed that eligible transaction in respect of trading in commodity derivatives carried out in a recognised association which is chargeable to commodities transaction tax shall not be considered to be a speculative transaction.

- **Disallowance on account of non-withholding of tax**

In the case of non-deduction / non-payment of tax at source made to residents, the disallowance of the expenditure will be confined only to 30% of such expenditure and not the full amount.

- **Investment Allowance**

Additional investment allowance at 15% to manufacturing companies that invests Rs. 25 crore in any year for next 3 years.

- **Taxability of Dividends from a Foreign Company**

The current provisions relating to taxation of gross dividends received by an Indian company from a specified foreign company at the concessional rate of 15% have now been proposed to be extended to AY 2015-16 and subsequent years.

- **Characterisation of Income in case of Foreign Institutional Investors (FIIs)**

It is proposed to amend the definition of "capital asset" to provide that any security held by FII which has invested in such security in accordance with the regulations made under SEBI would be treated as capital asset and income arising from transfer of such security would be taxable as capital gains.

- **Transfer Pricing**

APA rollback provisions introduced. Proposes "range concept" for ALP computation instead of arithmetical mean, except where adequate number of comparable are not available. Use of multiple year data to be allowed for transfer pricing benchmarking.

- **Retrospective Amendments**

All cases of indirect transfers arising out of retrospective amendments will be scrutinised by a high level committee of CBDT, before initiating any action.

- **Scope of AAR**

AAR scope to be expanded to resident private limited companies. This is a good indication for error-free and litigation free working.

E. Conclusion

The NaMo led government did try to ensure that no section of society or any part of the country is missed out in getting a mention in the Budget. However, the budget didn't provide clarity on GAAR, issue of bank recapitalisation, plan towards introducing the unified Goods and Services Tax (GST) and a concrete plan of rationalisation of subsidies (Food, fuel, fertiliser). The uncertainty created by retrospective taxation measures need to be permanently put behind.

The most awaited event of 2014 is behind us ..... equity market's attention would now move to global events, corporate earnings and real 'action' on the ground. Seems for now that the ACHHE DIN KEY lies in EFFECTIVE EXECUTION and IMPLEMENTATION.

This article is contributed by CA Niyati Hemani, Associate of K. T. Hemani & Co.
For any clarifications, kindly e- mail on niyati.ca@gmail.com or call on 98259 49076.