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FM shrugs off pleas by FPIs on super-rich tax

Finance Bill amendments propose further tax relief for startups, NBFCs

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NEW DELHI

The super-rich tax is here to stay for a large section of foreign portfolio investors (FPIs), with Union finance minister Nirmala Sitharaman ignoring their pleas while proposing further tax relief for startups and non-bank lenders.

In amendments to the Finance Bill proposed to Parliament and passed by the Lok Sabha on Thursday, Sitharaman added more safeguards against tax evasion.

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DOUBLING DOWN

The key takeaways fom the Finance Bill 2019 amendments cleared by the Lok Sabha:

- **FPIs SET** up as association of persons or trusts have to get converted to companies to avoid surcharge increase.
- **SCOPE OF** TDS on payments above ₹50 lakh extended to brokerage. For cash withdrawals above ₹1 crore, all bank accounts will be considered.
- **MORE CLASSES** of investors in startups are now exempt from the contentious angel tax. However, abusing tax relief will attract penalty.
- **THE AMENDMENTS** seek to boost entrepreneurial spirit by giving incentives to those starting businesses.

"FPIs organized as companies will not be affected by the increase in (highest marginal) tax rate and the fear of flight of FPIs from India is not well-founded."
NIRMALA SITHARAMAN, finance minister

The Union budget had proposed raising the income tax surcharge on taxpayers with income in the ₹2-5 crore range from 15% to 25%, and from 15% to 37% for those earning more. This takes the effective tax rate for those two groups to 39% and 42.74%, respectively.

Sitharaman emphasized that while tax concessions are being given to the middle class for buying affordable homes and for small to medium businesses and sunrise industries to promote growth, the affluent have to contribute more in taxes for nation-building.

Finance minister added more safeguards against tax evasion in the amendments to Finance Bill

"The essence of the taxation proposals in the Finance Bill are meant to promote ease of doing business, encouraging 'Make in India' and encouraging young entrepreneurs, who want to invest their own seed capital. That is the drive that 'Make in India' needs now, because there is a lot of enthusiasm among people who want to move from being in a salaried job to creating jobs for others," Sitharaman said in her reply to the discussion in the Lower House on the Bill.

The Bill retained the provisions to raise surcharge on income tax on wealthy individuals, despite FPIs organized as trusts claiming they are assessed as individuals and therefore, will be hit by the move. Quoting officials who advised her, Sitharaman said those FPIs were at liberty to adopt a corporate structure for which no surcharge increase was announced.

"FPIs organized as companies will not be affected by the increase. Only high-income individuals are covered by it and it is this government's policy that such individuals

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Sitharaman shrugs off pleas by FPIs on super-rich tax relief

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should contribute more for nation-building," said the minister.

The Finance Bill amendments sought to give relief to startups in terms of carrying forward their losses.

In a relief for non-banks facing a liquidity crisis, the Bill proposed that such lenders receiving interest from bad or doubtful loans would be taxed only on receipt of the income, not on an accrual basis, a method of recording transactions for revenue when earned and expenses when incurred. While giving concessions to startups, the Bill also proposed penalties for any abuse of such concessions, tax experts said.

The Bill also tightened the anti-evasion measures that were part of the original Finance Bill tabled earlier this month.

According to this provision, individuals have to deduct tax at source at the rate of 5% while making payments above ₹50 lakh as brokerage as well. The original bill had proposed this in the case of payments to contractors and professionals only.

Individuals have to deduct tax at source at 5% while making payments over ₹5 lakh as brokerage as well

The Bill also clarified that a proposal in the original Bill requiring a 2% tax to be deducted at source in cases where a person withdraws more than ₹1 crore a year from banks or cooperative banks or post office accounts applies to all accounts of that person taken together.

Rakesh Nangia, managing partner at Nangia Advisors (Andersen Global), explained that the amended proposal provides that if a person maintains more than one account with the same bank, the bank shall aggregate the withdrawals made from all such accounts to compute the threshold for tax deducted at source.

"The government is expanding the coverage of tax deducted at source rapidly," said Neeru Ahuja, partner at Deloitte India.

FPI SURCHARGE

Tax stays, investors told to convert

Lok Sabha passes Finance Bill with minor changes; 'no threat of investor flight', says FM

FE BUREAU
New Delhi, July 18

FINANCE MINISTER NIRMALA Sitharaman on Thursday declined to remove or relax the applicability of the new surcharge on the super rich on foreign portfolio investors (FPIs), but advised those staring at an increase in tax outflows to shift to the corporate structure where the Budget hasn't made any change in tax treatment.

Tax experts, however, said such a shift by FPIs using the trust structure would have been easier if the government had given them a one-time waiver from capital gains tax. Since many of these 'Trust FPIs' may also have considerable unrealised gains, the tax cost of conversion could dissuade them, the experts warned. Also, they said, such conversion might not be structurally possible in many jurisdictions from where the FPIs, which typically invest in India, operate.

"If the FPIs are registered as companies, they don't have the problem of higher surcharge on income tax. When it (FPI) is registered as a trust, which is treated as a taxable entity and therefore, as an individual entity, (it) comes under taxation. Many of our officials have also been (saying) that such FPIs who have registered themselves as trusts may consider the option of registering as a company," the minister said in the Lok Sabha, replying to the discussions on the Finance Bill. The minister asserted that the fear of flight of capital as a result of the move was "not well-founded".

More than a fifth of the FPIs investing in India equity, debt and hybrid instruments use the trust route.

The Bill was later passed by the lower House.

With the surcharge on categories of taxpayers with income above ₹5 crore rising by 22 percentage points, long-term capital gains tax on FPIs using the trust structure would now be 14.25% against 12% earlier; short-term gains would rise to 21.4% from 17.9%.

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Conditions apply

- Start-ups that are exempted from the angel tax to be penalised via a claw-back clause if they violate the very conditions for tax relief
- **More than one account with the same bank:** Withdrawals will be combined to compute the threshold for 2% TDS on withdrawal exceeding ₹1 crore a year
- While the Bill initially exempted a category-III AIF investing in an exchange in an IFSC from capital gains tax only if all the fund's investors were non-residents, waiver will now be available to funds with resident investors as well, subject to riders

FPI surcharge: Tax stays, investors told to convert

FPIs, including pension and retirement funds, educational endowment fund, etc, come in through trusts route because it has been the most tax-efficient structure. Typically, a corporate fund would have to pay MAT at over 18.5% and an additional 20% as dividend distribution tax. Despite the hike in surcharge, FPIs might find the trusts still the least taxing structure, although the post-tax returns in the hands of the foreign investors could fall. Given that emerging market like India provide better returns, most Trust funds could continue to invest in India; they would pull back only if other determinants like corporate earnings here and the fundamentals of the Indian economy compared with other nations also tend to turn worse.

"This (the advice to FPIs to convert to corporate structure) is likely to disappoint FPIs because it's not easy to restructure global funds only for Indian tax reasons. The government doesn't seem to appreciate that just as our mutual funds are formed as trusts because regulations require so, in various countries, funds are set up as trusts because of home-country regulations, industry practice and commercial reasons, and not because they saw an advantage in India earlier," said an analyst. He said a uniform rate for all FPIs because corporate or non-corporate status is entirely a home country creation.

FPIs remained net buyers in most part of 2019, having bought shares and local papers worth $13.08 billion so far this year. This compares with last year's sale of $4.6 billion in equity and $6.7 billion in bonds.

Sitharaman mooted a host of amendment to the Bill before it was put to voice vote. She clarified that only gift paid by a resident as money to a non-resident would be deemed to arise in India, even when the act of gifting occurs outside India. It has now been clarified that the 'gift' in the law pertains to money and not immovable property.

While the government had earlier exempted start-ups from angel tax contingent on the firms fulfilling certain condition, the amendment to Finance Bill, 2019, seeks to penalise the firms that violate such conditions by imposing claw-back clause in the law. Angel tax refers to the taxability of the amount which is the difference between the consideration received from issue of share and the fair market value of such shares.

"If a start-up claims exemptions from angel tax but subsequently buys, say, a motor vehicle, in contravention to the condition of notification issued by the DPIIT, it shall be liable to pay angel tax and 200% penalty on the tax sought to be evaded," Naveen Wadhwa, DGM, Taxmann, said.

Further, while the Bill initially exempted a category III alternate investment fund (AIF) investing on an exchange in an International Financial Services Centre from capital gains tax only if all the investors in the fund were non-residents, the waiver will be available to such funds even with resident investors on board, but only to the extent that gains are in respect to units held by non-residents. "The amendment recognises the fact that a resident sponsor or fund manager located at IFSC or elsewhere in India would also be required to hold investments in the fund. Hence, reacting to industry demand, it is now proposed to exclude such resident investors for the fund to qualify for capital gains exemption," a tax expert said.

On the proposed 2% TDS on cash withdrawal exceeding ₹1 crore in a year, the minister said that if a person maintains more than one account with the same bank, the bank is required to aggregate the withdrawals made from all such accounts to compute the threshold. "This amendment plugs the loophole only partially as a person can maintain various accounts with different banks and withdraw less than ₹1 crore from each such bank to avoid the TDS," said Rakesh Nangia, managing partner at Nangia Advisors (Andersen Global).

Sitharaman also told Parliament that the amendment to the RBI Act, proposed in the Finance Bill, was meant to enable the central bank's powers to effectively regulate Non-banking financial companies (NBFCs). The Budget also empowers the RBI to regulate housing finance companies (HFCs), replacing National Housing Bank, which will remain only a re-financier to the HFCs. A day after presenting the Budget, the finance minister had said the crisis in the shadow-banking sector seemed to have bottomed out even though woes of some players still persisted.

IL&FS default: NCLT allows govt to prosecute auditors Deloitte and BSR

Further, the tribunal also asked the corporate affairs ministry to implead Surinder Singh Kohli and Subhalakshmi Panse who were independent directors of IFIN and were part of the audit com-

The Finance Bill, 2019, said any bank or a co-operative society engaged in carrying on the business of banking; or post office, which is responsible for paying any sum, in cash, in excess of Rs one crore during the previous year, to any person from "an account" maintained by the recipient with it shall, at the time of payment of such sum, deduct an amount equal to 2 per cent of sum exceeding Rs 1 crore, as income-tax.

The Finance Bill amendment replaced "an account" to "one or more accounts".

Amendments also clarified that the total TDS paid on cash withdrawal beyond Rs 1 crore will be adjusted against the total tax dues from the taxpayer and would not be constituted as income in hands of the taxpayer. This provision would come into effect from September 1, 2019.

"I want to assure the members that if there are people who are taxpaying citizens, who have withdrawn like this, this TDS will be adjusted against the total tax dues," said Sitharaman.

"So, it is not over and above what he is expected to pay as tax, but it is going to be reconciled with the total tax claims which is going to be laid on this individual. So, it is not something which is running parallel to it," Sitharaman said while replying in the debate on Finance Bill.

Rakesh Nangia, managing partner at Nangia Advisors (Andersen Global), said there was a possibility that people may misuse the TDS provision by maintaining various bank accounts.

"The amended proposal provides that if a person maintains more than one account with the same bank, the bank shall aggregate the withdrawals made from all such accounts to compute the threshold. Though this amendment plugs the loophole but partially, since even not a person can maintain various accounts with difference banks and withdraw less than Rs 1 cr from each such bank to avoid the TDS," Nangia said.

Business Standard

Govt to levy 2% TDS on cash withdrawal over Rs 1 cr from multiple accounts

The total TDS paid on cash withdrawal beyond Rs 1 crore will be adjusted against the total tax dues from the taxpayer.

Press Trust of India | New Delhi July 18, 2019 Last Updated at 21:15 IST

The government will charge a two per cent tax if aggregate cash withdrawal from one or more accounts exceeds Rs 1 crore, according to an amendment made to a Budget proposal and announced Thursday.

Finance Minister Nirmala Sitharaman, in her Budget on July 5, had proposed 2 per cent tax deduction at source (TDS) on Rs 1 crore cash withdrawal from "an account" to discourage high-value withdrawals.

As people holding multiple accounts could have misused the proposal, the government amended the Finance Bill, 2019, to state that TDS will be charged if aggregate withdrawal from "one or more accounts" of a person exceeds Rs 1 crore.

The amendment, along with 28 others, were approved by a voice vote by the Lok Sabha, which passed the Finance Bill 2019.

SITHARAMAN'S REPLY TO DEBATE ON FINANCE BILL

FM Sticks to Proposals, No Relief to FPIs in Trust Form

Surcharge on **super rich** to apply to FPIs organised as trusts

Nearly **40%** FPIs will face this levy

60% FPIs organised as corporates not covered by surcharge

FM says FPIs **should convert** themselves into corporates to avoid levy

Says fears of capital flight due to higher tax surcharge baseless, asks affected FPIs to shift to company structure

Our Bureau

New Delhi: Finance minister Nirmala Sitharaman stuck to her budget proposals and declined to relent on the demand by foreign portfolio investors (FPIs) structured as trusts that they be exempted from a higher surcharge. She said they should adopt a company structure in order to avoid the surcharge. She also said the government believed that the richest should contribute more to society and nation building.

Fears that the surcharge would lead to a flight of FPIs were baseless, she told Parliament in her reply to the debate on the Finance Bill. The government's tax proposals are aimed at giving a greater push to Make in India, ease of doing business and young entrepreneurs who want to establish startups, she said.

"The fear of flight of FPIs from India is not well-founded," she said. "Increase in effective tax rate applies only to individual taxpayers, including other forms of FPIs such as trusts," she said, winding up the discussion on the Finance Bill in the Lok Sabha on Thursday. About 40% of FPIs investing in the country are structured as trusts or associations of persons (AoPs).

Experts said switching from a trust to a corporate structure wouldn't be easy

In the July 5 budget, Sitharaman had proposed to increase the surcharge levied on top of the applicable income tax rate to 25% from 15% for those with taxable incomes between ₹2 crore and ₹5 crore, and to 37% for those earning more than ₹5 crore. This takes the effective tax rate for those two groups to 39% and 42.74%, respectively.

The BSE Sensex has declined 2.5% since the budget.

Experts said switching from a trust to a corporate structure wouldn't be easy.

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Tax Risks Post Conversion

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"Most of the FPIs are global funds which invest in several countries and not just India and the trust structure is chosen either because of regulatory necessity in the home country or because the trust structure offers flexibility in terms of operational ease of setup and winding down, redemptions to investors, administrative compliance and legal compliance," said Rajesh H Gandhi, partner, Deloitte Haskins & Sells LLP.

Gandhi pointed out that a change in structure could require the vable property situated in India to a person outside the country.

The amended section now provides that only gifts of money paid by a person resident in India to a nonresident shall be deemed to arise in the country, even when the same is outside it.

Taxation arising on account of claw-back for startup companies that breach notified conditions will now be in respect of excess consideration over fair value. Initially, the Finance Bill had inadvertently provided for claw-back taxation by calculating excess of consideration

which would trigger not only capital gains tax in India but also other costs such as securities transaction tax, brokerage and forex costs since the regulator does not allow free-of-cost transfers.

"Further, there is always a risk that tax authorities could invoke General Anti-Avoidance Rules and disregard the conversion on the argument that it was done to avoid higher capital gains tax," Gandhi said.

Other tax experts echoed these views.

"No one in the government seems to appreciate that just as our mutual funds are formed as trusts because regulations require so, in various countries, funds are set up as trusts because of home country regulations, industry practice and commercial reasons and not because they saw an advantage in India earlier," said Sunil Gidwani, partner, financial sector, Nangia Advisors (Andersen Global).

"The migration to a corporate structure could also entail additional capital gains tax burden for the FPIs registered as trusts," said Punit Shah, partner, Dhruva Advisors LLP.

The Lok Sabha passed the bill by voice vote, completing the budget process for 2019-20 in the Lower House. It will now go to the Rajya Sabha. A money bill doesn't need Upper House approval.

Referring to the imposition of 1% tax deducted at source on cash withdrawals beyond Rs 1 crore, she said the tax could be adjusted against the liability of the assessees and hence there will be no additional burden on them. She also highlighted the budget tax proposals, including incentives to boost electric vehicles, startups and the corporate sector in her reply.

CLARIFYING AMBIGUITIES

The government also moved amendments on Thursday to clarify ambiguities over changes proposed in the Finance Bill. Gifts to persons outside India had been included in the ambit of income deemed to accrue or arise in India by the Finance Bill. The language of the new clause in Section 9 had led to some confusion since it used the term "person outside India," which is nowhere defined under the Act. Also, the proposed amendment included gifts of immo-

vided that once this taxation is act vated, there will be a penalty impo sed at the rate of 200% since the ex cess is deemed to be misreported c concealed income.

A significant amendment in the Fi nance Bill included withdrawal o tax exemption for charity in case o breach in provisions for achievin the objects of a charitable trus This provision has now been inclu ded to cover universities, hospital educational institutions.

Another change has been carrie out in the proposal related to catego ry III Alternate Investment Fund that invest on an exchange in inter national financial services centre The original proposal required a investors in the fund to be nonresi dents in order for the fund to be ex empt from capital gains tax. Bowin to industry demand, the govern ment has now made consequentia amendments to the Finance Bill t provide for exemption to the fun from capital gains to the extent ga ins are in respect of units held b nonresidents.

AMENDMENTS THROUGH FINANCE BILL

The Finance Bill involved amend ments to seven legislations each un der direct and indirect taxation t boost manufacturing and bring gre ater simplicity and effectiveness t the country's laws.

She said the amendments wer under five categories--direct taxe indirect taxes, Prevention of Mo ney Laundering Act (PMLA), fi nancial markets and central roa funds. Amendments were also be ing made to the Securities Cont ract (Regulation) Act, the Sebi Ac RBI Act, laws relating to insuran ce, bank nationalisation and th National Housing Bank. She sai the proposal to amend the Reserv Bank of India (RBI) Act will allow the central bank to regulate hou sing finance companies, as propo sed in the budget.

Of the eight PMLA amendment six pertained to explanations. Th amendment clarifies that a perso will be held guilty of money launde ring if found to have directly or in directly attempted to indulge o knowingly is a party to concea ment, possession, acquisition, us or projecting as untainted propert or claiming as untainted propert in any manner.

Finance Bill amends 7 direct & indirect tax laws

Black Money, I-T and Benami Acts among the laws that have changed

ENS ECONOMIC BUREAU @New Delhi

FINANCE Minister Nirmala Sitharaman said the Finance Bill 2019 passed by Lok Sabha on Thursday has amended seven direct and indirect taxation-related laws.

"The Bill is looking at various taxation proposals of the Centre for financial year 2019-20. Under the direct taxation, about seven Acts are being amended, keeping in mind the Make in India," she said.

The Payment and Settlement systems Act, Black Money Act, Income-Tax Act, Finance Act 2015, Finance Act 2004 and Benami Act are among the seven direct taxation laws that are being amended in the Bill.

According to Rajesh Gandhi, senior partner (direct taxation), Deloitte, "There are no significant changes in direct taxes... For start-ups, the way taxation on earnings from sale of shares is done has been slightly amended. Instead of taxing the difference between the fair market price and face value of the share, taxation is now between fair market price and consideration received from the sale of the share."

Earlier, the Finance Bill had included gifts to persons outside India under the ambit of income deemed to accrue or arise in India, but this led to a lot of confusion. "In order to remove the ambiguity, the amendment now provides that only gift of money paid by a resident in India to a non-resident shall be deemed to arise in India, even when the same is arising outside India," said Sunil Gidwani, partner (financial sector), Nangia Advisors.

The amendments in taxation laws include reduction in corporate tax rate; incentives to purchase of electronic vehicles, start-ups, international financial service centres and certain NBFCs; furthering the government's agenda on tackling black money; TDS on tax withdrawal from banks; compulsory returns filing; quoting of PAN and Aadhaar and so on.

Outgoing budget documents at the Parliament House on Thursday | SHEKHAR YADAV

No relief for FPIs unless they turn corporates

ENS ECONOMIC BUREAU @New Delhi

FOREIGN Portfolio Investors (FPI) can register themselves as companies to avoid the super-rich tax surcharge imposed in this year's budget.

FPIs that function as trusts in India will have to pay the tax surcharge proposed, said Finance Minister Nirmala Sitharaman on Thursday. She added that FPIs may consider the option of structuring as companies and FPIs functioning as trusts may consider being registered as companies.

The Finance Minister, in her Budget presented earlier this month, slapped an effective Tax Surcharge of 3 per cent for individuals with an annual income of between ₹2 crore and ₹5 crore, and 7 per cent for those earning more than ₹5 crore.

The additional taxes apply to individuals and groups of individuals who are an Association of Persons (AoP) or a body of individuals. The tax surcharge and realisation that it could apply to FPIs sent shock waves through bourses and saw stocks plunging last week.

The decision not to make any changes in the tax surcharge for FPIs is disappointing and may lead to loss of some business on the bourses and redeployment elsewhere

Amit Bannerjee, merchant banker

"The decision not to make any changes in the tax surcharge for FPIs is disappointing and may lead to loss of some business on the bourses and redeployment elsewhere," said Amit Bannerjee, an independent merchant banker specialising in East Asian Funds.

According to depositories data, overseas investors withdrew a net sum of ₹4,953.77 crore from equities during July 1-12, but poured in a net ₹8,504.78 crore into the debt market, translating into a cumulative net investment of ₹3,551.01 crore.

Budget surcharge stays on FPIs

OUR SPECIAL CORRESPONDENT

New Delhi: Finance minister Nirmala Sitharaman on Friday said foreign portfolio investors (FPIs) can register as companies to avoid the new tax surcharge imposed on individuals and trusts in the budget.

"The super-rich should contribute more to the society and nation building. FPIs should consider the option of structuring themselves as companies rather than trusts to avoid paying the increased surcharge," she said during a debate on the Finance Bill in the Lok Sabha. The bill was later passed by a voice vote.

Nirmala Sitharaman during the budget session of Parliament on Thursday. PTI

In the budget, Sitharaman had proposed to raise the surcharge on the super-rich. The surcharge on those with an annual income of Rs 2 crore to Rs 5 crore would be raised to 25 per cent from 15 per cent. For those earning Rs 5 crore or more annually, the surcharge was increased to 37 per cent from 15 per cent. With this, the effective tax rate will go up to 39 per cent for those in the Rs 2-5 crore income slab and 42.74 per cent for those in the Rs 5 crore and above group.

Sunil Gidwani, partner-financial services, Nangia Advisors (Andersen Global), said, "This is likely to disappoint FPIs because it is not easy to restructure global funds only for Indian tax reasons. No one in the government seems to appreciate that just as our mutual funds are formed as trusts because regulations require so, in various countries funds are set up as trusts because of home country regulations, industry practices and commercial reasons and not because they saw an advantage in India earlier."

A change of FPIs from trusts to companies would not be that easy as "under the general anti-avoidance rules, tax authorities can question the move and even deny tax benefits", Punit Shah, a partner at Mumbai-based tax consultant Dhruva Advisors LLP, said.