THE UNION BUDGET 2021-22

Homi P. Ranina

Forum of Free Enterprise

FORUM
OF FREE ENTERPRISE

"Free Enterprise was born with man and shall survive as long as man survives".

- A. D. Shroff
Founder-President
Forum of Free Enterprise

SHAILESH KAPADIA

(24-12-1949 – 19-10-1988)

Late Mr. Shailesh Kapadia, FCA, was a Chartered Accountant by profession and was a partner of M/s G.M. Kapadia & Co. and M/s Kapadia Associates, Chartered Accountants, Mumbai.

Shailesh qualified as a Chartered Accountant in 1974 after completing his Articles with M/s Dalal & Shah and M/s G.M. Kapadia & Co., Chartered Accountants, Mumbai. Shailesh had done his schooling at Scindia School, Gwalior and he graduated in Commerce from the Sydenham College of Commerce & Economics, Mumbai, in 1970.

Shailesh enjoyed the confidence of clients, colleagues and friends. He had a charming personality and was able to achieve almost every task allotted to him. In his short but dynamic professional career, spanning over fourteen years, Shailesh held important positions in various professional and public institutions.

Shailesh's leadership qualities came to the fore when he was the President of the Bombay Chartered Accountants' Society in the year 1982-83. During his tenure he successfully organized the Third Regional Conference at Mumbai.

Shailesh was member, Institute of Fiscal Studies, U.K.; member of the Law Committee and Vice-Chairman of the Direct Taxation Committee, Indian Merchants' Chamber. He was also a Director of several public companies in India and Trustee of various public Charitable Trusts.

He regularly contributed papers on diverse subjects of professional interest at refresher courses, seminars and conferences organised by professional bodies.

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Blueprint for a Post Pandemic Recovery

Homi P. Ranina*

The annual budget provides an opportunity for the Government to showcase its economic and financial strategies and policies, apart from presenting to its citizens the receipts and expenditure statement for the year under review. The Finance Minister's job was cut out requiring her to do a fine balancing act to take care of several conflicting and complex challenges, given the backdrop of the corona virus once-in-a-lifetime pandemic.

Budget 2021-22 must not be looked at in isolation. It is a cumulative effort of the five 'mini budgets'

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announced in 2020. The fiscal deficit of 9.5% for the current financial year 2020-21 reflects the onerous financial strain on the country's economy as a result of a precipitous fall in tax revenues due to the economic lockdown and unforeseen expenditure on healthcare services.

The budget document reflects a progressive vision of the roadmap to faster economic recovery focusing on the six strategic pillars of infrastructure, innovation, research and development, human capital, inclusive growth and the oft repeated phrase 'minimum government, maximum governance'. The National Infrastructure Pipeline has been enlarged to cover 7,400 projects. This, coupled with the setting up of economic corridors, expansion of highways, public transport and investment in railways, will help provide easy access to raw materials, generate more employment opportunities and bring the physical infrastructure to world class standards.

Budgetary arithmetic

The fiscal deficit for 2020-21 is estimated to be Rs. 18,48,655 crore which is 9.5% of the GDP, breaching the mandate of the Fiscal Responsibility and Budget Management Act. This is on account of a dramatic fall in collection of direct and indirect taxes. The only silver lining on the dark cloud has been the recovery of Rs. 85,000 crore from about one lakh tax payers under the Vivad se Vishwas scheme announced by the Government last year which will also result in a fall in pending litigation before various Courts and appellate authorities.

Low tax revenue collection has always been and continues to be the Achilles Heel of the Indian economy. The gross tax revenue which is estimated to be collected during the fiscal year 2021-22 is Rs. 22,17,059 crore. This gross tax revenue collection is around US$ 296 billion which is much less than what many large multinational corporations earn in revenue every year. After transferring funds to State governments and Union Territories, the net tax revenue which will remain with the Central Government will be Rs.15,45,397 crore.

The Government's collection by way of the Goods & Services Tax is estimated to be Rs.6,30,000 crore. Corporate tax will fetch Rs.5,47,000 crore and personal income-tax Rs.5,61,000 crore. Customs and excise duty put together will bring around Rs.4,71,000 crore. Thus, the Government has to rely substantially on non-tax revenues and market borrowings in order to fulfill the expenditure target of Rs.34,83,236 crore.

The gross domestic product (GDP) for fiscal year 2021-22 is pegged at a figure of Rs.223 lakh crore which is roughly US$ 2.97 trillion. The fiscal deficit is projected to be Rs.15,06,812 crore which is 6.8% of the GDP during this fiscal year. This deficit will add to the public debt of the Indian Government resulting in an interest burden of Rs.809,701 crore on the outstanding debt. Defence expenditure on revenue account is estimated at Rs.347,088 crore.

The Government has raised capital expenditure by 25% despite the resource crunch. There is a sharp increase in such expenditure for the fiscal year 2021-22 for which a provision of Rs.5,54,000 crore has been made, which is an increase of 34.5% than what is the estimated expenditure of fiscal year 2020-21. Of this, Rs.44,000 crore is to be spent on projects and programmes which are under implementation so that they can be completed at an early date. The increased Government capital expenditure will compensate for the fall in capital expenditure incurred by the private sector which has remained sluggish even after the lifting of the lockdown. The Finance Minister has also indicated that she will come up with a specific mechanism to encourage State Governments to spend more by way of capital expenditure on creating new infrastructure facilities.

Indirect taxes conundrum

While Goods & Services Tax collection is showing an upward trend as a result of stringent administrative measures, the International Monetary Fund has assessed the effective tax rate of GST at 11.8%. This is close to the Reserve Bank of India's estimate of 11.6%. This is considerably lower than the 14% average revenue neutral rate which was fixed for smooth transition from the Value Added Tax regime without any revenue loss. GST's true potential is to generate revenue at 7.1% of GDP, while at present it generates revenue of 5.1% of GDP. At current levels, this translates into a revenue loss of roughly Rs.4 lakh crore. The 15th Finance Commission headed by Mr. N.K. Singh has suggested that the 12% and 18% slabs be merged into one standard rate and that GST be rationalized to a three rate structure complemented by the 5% merit rate and the 28% demerit rate.

To increase measures for tax compliance, quarterly return filing and monthly payment of GST for small tax payers has been introduced. An electronically generated invoice will help small retailers who will also be provided with a pre-filled tax return which can be edited. The input tax credit statement will have to be validated and the capacity of the GSTN system has been enhanced. To identify tax evaders and those who declare lower turnover and sales, tools of artificial intelligence and deep analytics are to be put in place.

Customs duty is proposed to be rationalized with the twin objectives of promoting domestic manufacturing and helping India to get into the global value chain which will promote exports. About eighty outdated exemptions are sought to be eliminated. A revised customs duty structure is to be put into place from 1st October, 2021 after reviewing more than 400 old exemptions. Under the new policy, all customs duty exemptions announced hereafter will be valid for two years only from the issue date. Thereafter, these exemptions will lapse unless they are revalidated.

Resource mobilization through monetization of assets

The Finance Minister has worked on the principle that expenditure stimulus through higher outlays of capital expenditure of Rs. 554,000 crore will provide the backward linkages with industry and create more jobs. Government has indicated that it will recover Rs.1,75,000 crore during fiscal year 2021-22 through the disinvestment process and by monetizing Government assets, being surplus land of public sector companies. According to data available, there are 46 public sector units which hold surplus land at a figure of Rs.47,000 crore which is the original cost of the land. The current market price would be substantially more than this figure. Implementation of this proposal may be partially successful given the fact that documents pertaining to the land titles may not be available or may be defective. Further, some plots of land may be under dispute which cannot be disposed of immediately.

A National Asset Monetization Pipeline has been announced by the Prime Minister who is in favour of reducing ownership stake by the Government in public sector enterprises. He has personally invited foreign investors to participate in the privatization process, offering more than a hundred projects in the oil, gas, ports, airports and power sectors. The new mantra is to monetize and modernize national assets based on the principle that the Government should not be involved in any business enterprise: 'the business of the Government is to govern, and not to do business'.

With a view to curtail Government spending, subsidies have been reduced by 43%. The food, fertilizer and petroleum subsidies for 2021-22 are at a lower figure of Rs.335,361 crore as against the estimated figure of Rs.595,355 crore for the fiscal year 2020-21.

Agricultural landscape

The Government has been re-mandating the agricultural landscape to double the income of farmers and to bring out their entrepreneurial spirit. The roadmap aims at higher productivity linked increase in output, rationalization of production costs, diversification into high value items and increasing the remunerative prices of agri products. The total amount allocated for the agricultural ecosystem is Rs.1,37,088 crore which includes allocations for animal husbandry, dairy farming, fisheries and food processing industries. The budget proposals enhance the availability of credit to this sector by pegging it at Rs.16.5 lakh crore. Further, the interest subvention through Kisan credit cards will now be available on crops, animals and fisheries, making this facility more inclusive.

The resilience that the agricultural sector has shown during the difficult Covid phase has been recognised in the budget speech by earmarking substantially higher resources for this sector. There has been emphasis on post-production management including marketing and risk negotiation, buttressed with technological inputs. The higher allocation for infrastructure will also result in pumping money into the rural sector, thereby creating additional jobs.

To get the additional resources, the budget has proposed an Agriculture Infrastructure and Development Cess which will apply to over a dozen items, like gold, silver, alcoholic beverages, crude palm oil, urea based fertilizers, etc. Petrol and diesel will also become subject to the cess of Rs.2.5 a litre and Rs.4 a litre, respectively. However, the basic customs duty and additional excise duty on these fuels will be proportionately reduced. Hence, there will be no net impact on the final consumers of these products.

A whopping sum of Rs.423,000 crore has been earmarked by way of food subsidy for the fiscal year 2021-22. This is in view of the commitment of the Government to continue with the Minimum Support Price (MSP) regime and increase procurement of food grains from farmers, thereby allaying their fears that the new farm laws recently enacted by Parliament will do away with the MSP. The public procurement of paddy, wheat and cotton has increased substantially in the past few years and the procurement of pulses has increased by more than forty times over the last six years.

Development of infrastructure

The Government has in earnest embarked on infrastructure projects, some of which are partially complete. In order to give a boost to capital expenditure, the highest allocation of Rs.1,08,230 crore has been earmarked for the Ministry of Road Transport & Highways. The total capital expenditure for infrastructure development has been pegged at Rs. 5.54 lakh crore for the fiscal year 2021-22, which is a 26% increase over the estimated spending of Rs.4.39 lakh crore for the financial year ended on 31st March, 2021. To further augment the road transport infrastructure, more economic corridors have been announced which would lead to new satellite cities and towns cropping up along the corridors. In order to promote public-private participation, it is proposed to invite investments in the Metro Rail network and public bus transport services. Private players will be permitted to finance, acquire, operate and maintain these services, primarily in the Tier-2 and Tier-1 cities.

Apart from the physical infrastructure, the Government has also emphasized the need for promoting the social infrastructure by allocating funds for the health care and education sectors. Most analysts believe that there is a lot of global money waiting to come into India as a result of improving economic indicators. Thus, significant flows of foreign direct investment are expected. To boost the social infrastructure, Rs.50,000 crore have been allocated for providing tap water connections to 28.6 million households and a further amount of Rs.60,030 crore has been allocated for drinking water and sanitation.

To boost the viability of power distribution companies, a new distribution scheme is launched with an outlay of Rs.305,982 crore which is to be spread over the next five years. This scheme will provide assistance to distribution companies for creating the necessary infrastructure, including prepaid smart metering and feeder separation.

For modernization of Indian Railways, Rs.1.10 lakh crore has been allocated. In addition monies will be borrowed by the Indian Railways Finance Corporation to the tune of Rs.65,258 crore. Railways will also raise funds through monetization of the Dedicated Freight Corridor assets. In addition funds will be raised through disinvestment of the Container Corporation of India. The Western dedicated Freight Corridor and the Eastern dedicated Freight Corridor are projected to be commissioned by June 2022. To ensure their timely completion, an amount of Rs.16,086 crore has been allocated to the Dedicated Freight Corridor Corporation of India. The ability of the Government to execute these projects remains to be seen. To a great extent, this will depend on the private sector's willingness to participate in different projects which have been allocated and the speed with which the Dedicated Freight Corridors are commissioned.

Financial sector reforms

A professionally managed and adequately capitalised Development Finance Institution will help to bring to fruition the scores of projects under the National Infrastructure Pipeline and reduce pressure on banks. Notified infrastructure debt funds with the proposed tax benefit on zero coupon bonds should make them attractive to investors. In order to provide incentives to participants in the corporate bond market, a permanent institutional framework is being created to purchase investment-grade debt securities. Infrastructure debt funds will now be able to issue zero coupon bonds. Protection of small borrowers continues to be a priority of the Government as it has reduced the threshold for minimum loan size to Rs.20 lakhs in order to trigger the debt recovery process under the SARFAESI law.

A new Investment Charter is proposed to be introduced. This will standardize, rationalize, and provide clarity to ensure that service standards are implemented. An initial public offering by the Life

Insurance Corporation of India will potentially be the largest capital offering by the Government, resulting in a huge windfall which will add to the collection of non-tax revenues. It is apparent from the budget proposals that there is a determination to pursue growth even if it means a temporary fiscal slide back caused by the relatively high fiscal deficit. It is necessary for the Government to create enough space for revival of the economy.

Sops for individuals and entrepreneurs

The salutary part of the budget proposals is that the tax structure has been left untouched which has come as a relief to individuals who feared that a Covid tax/cess may be levied. Senior citizens who are more than 75 years old will not have to file income-tax returns if they have income only from pension and interest. Unfortunately, dividends have not been included. Therefore, those senior citizens who receive even a small amount by way of dividends from companies will still be liable to file the tax return. This proposal will benefit very few seniors because if refund has to be claimed in respect of the tax deducted at source, filing of the return is mandatory. Further, it has been clarified that seniors earning interest from multiple banks will be required to file the tax return.

A new dispute resolution mechanism for small direct tax payers is sought to be introduced with the object of resolving tax disputes without going through the normal appellate process. A panel of about 200 persons, comprising of retired Judges and former tax officials, will be set up. Whenever an application for dispute resolution is filed by a tax payer, the case will be allocated to two such experts chosen randomly from the panel. The entire exercise will be conducted in a faceless manner through the digital route.

Among the measures to improve compliance, it is proposed to levy a higher rate of tax to be deducted at source when payment is made to those who are not filing their tax returns. Interest which is currently fully exempt in the hands of high net worth individuals will become taxable if the annual contribution in unit linked insurance plans and the employees' provident fund exceeds Rs.2.5 lakhs.

The budget has sought to incentivize the incorporation of One Person Companies. This is expected to boost the startup and innovation ecosystem. It will provide total control by the promoter, lesser compliance burden and limited liability to the founder of the company. The definition under the Companies Act, 2013 of 'small companies' is proposed to be changed by increasing their thresholds for paid-up capital to Rs.2 crore from Rs.50 lakhs and in respect of turnover to Rs.20 crore from Rs.2 crore. This move will benefit more than two lakh companies and make it attractive for first time entrepreneurs to set up their business by incorporating a company rather than as a sole proprietor.

Non-resident Indians are encouraged to set up these companies in India which would incentivize new startups. For those which are set up by 31st March, 2022, tax holiday provisions would apply. The corporatisation of the startup will enable the entrepreneur to avail of finance from angel investors and venture capitalists. This will help them to scale up and grow.

Since lakhs of small entrepreneurs are in the textile business, the Government is determined to set up Mega Investment Textile Parks. Appropriate infrastructure will be put in place with plug-and-play facilities. Seven such parks are to be established in the next three years. The objective is to enable the textile industry to attract large investments, become globally competitive and boost employment generation. The apparel sector will specially benefit when units are set up in these parks.

A special portal is being set up where construction workers and gig workers can register themselves. They will be eligible for minimum wages, cover under the Employees' State Insurance Corporation and food schemes which are currently applicable for migrant workers. For employers, the compliance burden will be restricted to a single registration and licensing format, with a provision to submit annual returns online.

For small businessmen who carry on their trade and other activities, where 95% of the transactions are through the digital route, the requirement for tax audit will be applicable only if the turnover exceeds Rs.10 crore. Businesses having a turnover not exceeding Rs.2 crore can adopt the presumptive taxation method by treating only 6% of the turnover as their taxable income and pay tax thereon at the applicable rates. In such cases, their tax returns will be accepted without any enquiry or scrutiny. A person earning commission, brokerage or carrying on any agency business will not be entitled to avail of this presumptive form of taxation.

Affordable housing remains the Government of India's favoured segment in real estate. For the home buyer, the extension of the deadline by one more year up to 31st March, 2022 for the additional tax deduction of interest up to Rs.1.5 lakhs on loans taken to buy a house has been well received. Those who develop affordable housing projects will also get tax holiday for one more year. Tax exemption given to notified affordable housing projects for migrant workers is a positive step from a social security perspective.

Wooing foreign investments

The Finance Minister has announced a bold policy to encourage foreign funds to shift their base from tax havens to India. Complete tax exemption is sought to be given to offshore funds for shifting their assets to India and relocating in the International Financial Services Centre, such as the Gift City in Gujarat. There will be a zero tax rate on transfer of assets from other countries to India. Further, there is a ten-year tax holiday in respect of income earned by foreign funds located in the Gift City. This will help to develop IFSCs and will encourage offshore funds to relocate to these centres by 31st March, 2023. Currently, funds aggregating to billions of dollars, having underlying Indian assets, are based in Mauritius, Singapore, Dubai, Cayman Islands and other tax friendly locations. Gift City offers more tax incentives than such jurisdictions do.

Further, tax exemption has been given to foreign funds investing in real estate investment trusts and infrastructure investment trusts. Since the dividend distribution tax has now been removed and the dividends will be taxed in India in the hands of the shareholder company, credit would be available to the foreign funds in respect of the tax paid in India against the tax payable on the income in the country of their residence. Dividends will now be taxable in the hands of foreign portfolio investors at the lower rates prescribed by the relevant double tax avoidance agreement. These rates vary from 5% to 15% whereas the standard rate under the Indian tax law is 20%. This will do away with the hassles faced by foreign portfolio investors to claim refund of excess tax which was deducted at source earlier by Indian companies.

Banking and insurance sectors

The Central Government has laid down a roadmap for privatization of public sector banks, two of them to start with. This will improve credit growth, bring in better operational efficiencies and attract fresh investments which will help these banks to recapitalize themselves. A new asset reconstruction company, popularly referred to as a ‘Bad Bank’, will be set up to help banks to tide over the wave of Covid-19 related bad loans. The new company will take over the stress debts and other assets which will thereafter be disposed of in a transparent manner to Alternate Investment Funds and other potential investors.

Insurance is an important route through which the Centre can raise long term finance. Therefore, it is proposed that the foreign direct investment limit in insurance companies be raised from 49% to 74%. Apart from this, management rights would be given to foreign investors and the Government will take a back seat though it will continue to hold 26% of the equity capital of insurance companies.

Though there is not much room for cheer for middle class tax payers, the stock market has responded positively. Some may consider the steep rise in stock prices as ‘irrational exuberance’. However, market analysts are looking at the performance of the corporate sector during the financial year 2021-22. Most companies will record a hefty rate of growth in view of the low performance index of 2020-21.

Further, the ready availability of liquid funds in the global market has boosted the flow of funds from foreign portfolio investors. With interest rates coming down on debt instruments, the stock market seems to provide an attractive avenue for investment. Needless to add, the growth of the

Indian economy will alone justify the phenomenal rise in stock prices.

V-shaped recovery on the anvil

The recent recovery of the economy is triggered by the increase in Government expenditure and pent up consumption demand among the middle and high income groups. There is some sign of acceleration in retail lending as mobility and normalcy return to the economy. By and large, the budget is transformative in nature. It is gradually demolishing the citadel of public sector through strategic disinvestment. Given the pandemic challenges, it needs to be stressed that one should not be perturbed by the relatively high fiscal deficit.

It is necessary for the Government to create enough space for revival of the economy, strengthening the health infrastructure, and provide for other social needs. The real challenge was to formulate the appropriate strategy for raising resources and for determining spending priorities. The big ticket announcement is that of accelerated disinvestment of public sector entities and increasing the stake of foreign and domestic investors in such entities so that effective decision making is out of Government control.

The increase in market borrowings is a cause for worry as public debt will snowball and the burden of interest payable thereon will fall on future generation Indians. Raising taxes from those who have concealed income together with interest and penalty would be one way to reduce dependence on market borrowings. The ultimate solution for reduction of public debt is to raise resources from those who have continuously evaded taxes during the past few years. Tax compliance both on the direct and indirect front is the only sure way to ensure fiscal prudence and bring down the fiscal deficit over the next three years.

The Finance Minister has shown remarkable determination to pursue growth even if it results in breaching the fiscal deficit numbers. The hope is that more growth will lead to more jobs, more self-employment opportunities, reduce poverty and kick-start the manufacturing sector which in turn will bring more revenues by way of direct and indirect taxes. This has resulted in boosting the investment sentiment.

According to the International Monetary Fund, India accounts for about 7% of the world GDP based on purchasing power parity terms. For the financial year 2021-22, the IMF has projected a rate of growth of 11.5%. Most market analysts believe that India's financial architecture will greatly strengthen in the coming months as a result of the budget proposals and the Indian economy will get back on its feet earlier than expected. The key to growth will be to bring to fruition the schemes for which funds have been allocated. Implementation of the proposals will alone ensure that there is a trajectory change in India's growth path and the vision of a 5 trillion dollar economy is translated into reality sooner than later.

The views expressed in this booklet are not necessarily those of the Forum of Free Enterprise.

“People must come to accept private enterprise not as a necessary evil, but as an affirmative good”.

- Eugene Black
Former President,
World Bank

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The Forum of Free Enterprise is a non-political and non-partisan organisation started in 1956, to educate public opinion in India on free enterprise and its close relationship with the democratic way of life. The Forum seeks to stimulate public thinking on vital economic problems through booklets, meetings, and other means as befit a democratic society.

In recent years the Forum has also been focusing on the youth with a view to developing good and well-informed citizenship. A number of youth activities including elocution contests and leadership training camps are organised every year towards this goal.

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