Opinion

THURSDAY, SEPTEMBER 26, 2019

NO COUNTRY FOR...

BJP leader, Kailash Vijayvargiya

As the national general secretary of BJP, I want to assure all of you that NRC will be implemented but not a single Hindu will have to leave the country. Each and every Hindu will be given citizenship

Listen to Greta Thunberg

Swedish teen activist highlights the urgency of climate action, the future will be bleaker if her message is ignored

WHAT SWEDISH TEENAGER Greta Thunberg—who is travelling the world when, in her words, she should have been in school—is pleading, and why, is far more important than the how of it. Thunberg made a passionate plea for urgent climate action at the United Nations Climate Action Summit in New York, and lashed out at world leaders for dithering. "You have stolen my dreams and my childhood with your empty words... We are in the beginning of a mass extinction. And all you can talk about is money and fairytales of eternal economic growth. How dare you!" Thunberg raged. There are many who have criticised the style and substance of Thunberg's activism before, and many more joined the list after her angry speech. Some commentators, nearly all of them climate-sceptics, have not-so-subtly brought up Thunberg's autism, and depression in attempts to blight her activism, and the overall stance of urgent climate action. Some others believe that the immediate action that Thunberg is urging will undermine democracy as the world knows it, and raise bogeys of climate action somehow fuelling populism—of the trade protectionism and anti-immigrant kinds that are rife today, championed by known climate sceptics. There are also some who endorse the substance of Thunberg's stance—time is running out to act on climate change, and future generations will greatly suffer if those in power today fail to take action—but, believe that Thunberg's methods are more panic-mongering than a reasoned call to action. Whatever the criticism, there can be no doubt that Thunberg is right in foregrounding climate action, rather than climate negotiations and deals, as the need of the hour.

Nearly all of the developed world seems to be still going soft on climate action. As per the Climate Action Tracker, only seven nations—India, Morocco, the Gambia, Ethiopia, the Philippines, Costa Rica, and Bhutan—are on action paths that are "2ºC compatible", that is, if all countries were taking similar action, it would be possible to realise the Paris goal of keeping warming to <2ºC from pre-industrial levels. But, a report by United in Science, a coalition of prominent climate science research institution, released just before the UN Climate Action Summit has sounded the foghorn—greenhouse gas emissions reduction must be at least tripled, and increased by up to fivefold if the world is to meet the Paris 2015 goals. Current plans take the world to average temperatures of between 2.9ºC and 3.4ºC by 2100, which could cause catastrophic change. Ahead of the summit, UN secretary general Antonio Guterres exhorted world leaders to take more coordinated action; "we have no time to lose," he said, as all manner of extreme weather and weather-related events—long heatwaves, record-breaking downpour and floods, raging wildfires, glaciers getting wiped out, etc—have played out in alarming frequency in the last few years. There is overwhelming evidence that the climate crisis has deepened over the past three decades, with the last one witnessing drastically accelerated impact.

A report by the Intergovernmental Panel on Climate Change last year said that the world has nearly run out of time for action—it is now hotter than pre-industrial levels by 1ºC, and will soon be hotter by 1.5ºC. At 1ºC of increase, we are already seeing untold devastation. In such a scenario, it is likely that Thunberg, who is seen by some as the voice of climate conscience that the world needs at the moment, has come to the stage too late. But, however bad the future that faces us, it will be much worse if we ignore what she is saying.

Benchmarking hurts banks

New loan pricing norms will hit their margins

With two significant events ahead, the Bank Nifty has crashed by close to 1,000 points over two trading sessions, with the State Bank of India (SBI) stock losing 10%. Investors' concerns are justified because once banks link interest rates—mainly home loans—and MSME loans to a benchmark from October 1, spreads will be under pressure.

The loans are to be benchmarked to the repo rate, the yield on the 3-6 month government bond, or certain other external benchmarks. With a chunky cut expected at the next monetary policy meet—Reserve Bank of India (RBI) is expected to reduce the repo rate by anywhere between 25 and 30 basis points—loan rates could fall further. It is not just new loans, even existing borrowers may be allowed to switch over, which means almost the entire portfolio will be repriced at lower rates. That is certain to crimp margins.

RBI's objective in asking banks to switch to an external benchmark is to bring about faster transmission; in the past, the cuts in the repo rate have not resulted in matching cuts by banks. To be sure, transmission has been slow partly because in 2015 and 2016, liquidity in the system was low; also, the NPA problems persisted, eating up capital, and lenders understandably preferred to wait until they were able to bring down the cost of deposits.

As liquidity became more abundant, loan rates fell and given how it has been in a big surplus of close to ₹1.5-2 lakh crore over the past few months, rate cuts would have followed. RBI, however, is clearly unwilling to wait.

There is also some concern that customers once used to rates falling find it difficult to cope when interest rates go up, often extending the tenure of the loan rather than paying a bigger EMI. In many ways, therefore, at times like this, when we are closer to the bottom of the repo rate cycle, the current loan rates could be much like teasers. Banks might, therefore, go slow on long-term products, and wait for interest rates to settle down, and we could see volumes thinning. Otherwise, with the interest rate on deposits not floating in nature, net interest margins (nims) could contract substantially. For instance, SBI's home loan is currently priced at about 8.1%, so, a cut in the repo would see an equivalent change in the loan rate. Once SBI drops the rate, other lenders would need to follow suit to stay competitive. Indeed, the SBI management has conceded that pricing the risk premium for a long term product like a home loan—25-30 years—is not easy and that managing the liabilities will be a challenge.

AppTURN

Govt makes it easier for farmers to rent machinery to remove crop-stubble via an app

BEGINNING EVERY OCTOBER, as farmers in Punjab, Haryana, and western Uttar Pradesh set fire to paddy residue, or crop stubble, to clear their fields for the rabi sowing season, smoke and particulate matter causes the Air Quality Index (AQI) in the Delhi-NCR region to spike to an average of 250-plus—well past the 'poor' level. Add to this the festival season, and the national capital region sees cases of severe respiratory distress spike to tens of thousands. Many solutions, ranging from banning crackers to providing low-cost protective face masks, have been tried out. Punjab CM Amarinder Singh recently suggested that suitable compensation could encourage farmers to desist from stubble burning, since the alternative—hiring a combine harvester—costs these farmers too much. Now, the central government has come up with a strategy to make more environment-friendly alternatives to the practice of stubble burning available to farmers in the NCR more easily, and at competitive costs.

The government has launched the CHC Farm Machinery app that allows farmers to both rent and buy, among other machinery required for farm work, equipment for in-situ management of stubble from custom hiring centres (CHCs) within a radius of 50 km. According to the ministry, 40,000 CHCs have registered with the app to make available 120,000 agricultural machinery at affordable rates. The app would allow farmers to know which hiring centres are available near them, see photographs of the machinery they wish to hire, and negotiate prices before placing an order. With the NCR already bracing itself for the onslaught of air pollutants, this digital solution to a long-continuing problem is a breath of fresh air.

SUSTAINABLE GROWTH

CHINA'S SUSTAINABILITY STRATEGY IS AN EXAMPLE OF GLOBAL LEADERSHIP. IN THE RUSH TO DEMONISE CHINA OVER TRADE, THE WEST HAS MISSED THIS POINT ALTOGETHER

Sustainability with Chinese characteristics

STEPHEN S ROACH

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Views are personal

IN THE HERE and now of climate change, it is easy to lose sight of important signs of progress. China, the world's biggest emitter of greenhouse gases, is a case in point. By changing its economic model, shifting its sources of fuel, developing new transportation systems, and embracing eco-friendly urbanisation, China's sustainability strategy is an example of global leadership that the rest of the world should consider very carefully. In the rush to demonise China over trade, the West has missed this point altogether.

In the past 12 years, China's economic structure has shifted dramatically from excessive reliance on smokestack manufacturing industries to low-carbon services. Back in 2006, the so-called secondary sector of GDP—largely manufacturing but also including construction and utility production—accounted for 48% of Chinese GDP, while the tertiary, or services, sector accounted for just 42% of GDP. By 2018, the shares had been reversed—41% of GDP for the secondary sector and 52% for services. For large economies, structural changes of this magnitude in such a short period are virtually unprecedented.

This shift was no accident. In March 2007, former Premier Wen Jiabao famously warned of a Chinese economy that was becoming increasingly "unstable, unbalanced, uncoordinated, and *unsustainable*." This sparked a vigorous debate over sustainability risks that had a major impact on China's most recent five-year plans and reforms. The leadership concluded that the Chinese economy could no longer afford to stay the energy- and pollution-intensive course set by Deng Xiaoping's hyper-growth gambit in the early 1980s.

Consistent with this dramatic structural transformation, China has been aggressive in shifting the mix of its fuel consumption away from carbon-intensive coal to oil, natural gas, hydro, and renewables. Although coal still accounted for 58% of China's total primary energy consumption in 2018—more than three times the 18% share in the rest of the world—that is down sharply from 74% in 2006, the year before Wen's "Four Uns" first drew serious attention to sustainability.

Significantly, China is leading the world in embracing non-carbon renewables such as wind, solar, and geothermal biomass. In 2018, China's renewables consumption was 38% larger than that in the United States and triple that of Germany. While renewables still account for just 4% of China's total primary energy consumption, they have been growing by 25% annually over the past five years (including 29% growth in 2018). If China remains on this path, then renewables could hit 20% of China's total energy consumption by 2025—a major breakthrough on the road to a cleaner, less carbon-intensive economy.

China's rapidly changing transportation model is a third key component of its sustainability strategy. China has the world's largest high-speed rail network, the fastest-growing subway system, and is leading all efforts in the rush to embrace electric vehicles. According to World Bank estimates, China is expected to exceed 30,000 km (18,641 miles) of installed high-speed rail by next year, up from more than 25,000 kms by 2017, and to add considerably more in the years ahead. This energy-efficient mode of long-distance connectivity stands in sharp contrast to the carbon-intensive transportation network created the US interstate highway system in the 1950s and 1960s.

Finally, the urban environment—obviously critical to any sustainability challenge—is especially, important in China where rapid urbanisation still has about three decades to go, with the urban share of its population likely to rise from nearly 60% at present to 80% by 2050. Yes, as in other countries, roads in China's major cities are severely congested. But, China is doing something about it, boasting seven of the world's 12 longest subway networks. Moreover, China's electric vehicles (EV) market dwarfs those elsewhere, with sales of over 500,000 EVs in 2017, versus slightly less than 200,000 in the US and Europe. And China's EV lead is projected to widen considerably over the next decade.

> **While renewables still account for just 4% of China's total primary energy consumption, they have been growing by 25% annually over the past five years**

China also stands out for its focus on a new eco-city urban model, featuring low-energy construction materials, light mass transportation, and well-planned "green space" urban pockets. The Xiong'an New Area, planned as a "subsidiary centre" south of Beijing, is particularly noteworthy in this regard, as is the existing Sino-Singapore Tianjin Eco-city and Hainan's recently announced plan to shift to all clean-energy vehicles. According to one recent estimate, China currently has plans to construct over 250 eco-cities. As a relative latecomer to urbanisation, China has the opportunity to rely on new models of city planning and energy efficiency that were not available to the first movers in the industrial world.

Is all this enough to make a difference for China and the planet? The good news is that China's share of global emissions has flattened out, albeit at a high level. China's share of global carbon dioxide emissions doubled from 14% in 2001 to 28% 2011, but has not increased since. While China's CO2 emissions did rise by 2.2% in 2018, that was less than in the US (2.6%), Russia (4.2%), and India (7.0%) while falling well short of outright declines of 1.6% and 2% in Europe and Japan, respectively.

Alas, the good news in China is probably not good enough for a planet that many judge to be already in crisis. It is one thing to bend the curve and stabilise the emissions *share*. It is a different matter altogether to achieve the 20% reduction in the *level* of emissions as originally stipulated in the 2015 Paris climate agreement. Nonetheless, by shifting away from carbon-intensive manufacturing to low-energy services, and embracing EVs, high-speed rail, and eco-friendly urbanisation—and likely to stay the course on all these trends—China is setting a high bar for the rest of the world.

While the trade war is important, China is winning the far more important battle for sustainability. To its credit, China is focusing on this battle at a point when its *per capita* output is barely more than one-third the level in the so-called advanced economies. A relatively poor country has made a conscious choice to shift its focus from the quantity to the quality of growth.

What about the rest of us?

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Gig economy needs a new labour gig

Court intervention can do little, as it cannot change the fundamental assumptions on which labour laws have been drafted

SARAYU NATARAJAN & ALOK PRASANNA KUMAR

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CALIFORNIA RECENTLY PASSED an important legislation classifying gig economy workers (such as Uber drivers) as "employees" of the platforms on which they seek work, that is, only if such companies have control over the hours and nature of work. Workers can, now, claim benefits under existing labour laws. While labour groups hail this as a victory, platforms claim that this will reduce flexibility.

The legislative intervention comes at an important juncture in history. The future of work, and workers, is poised to change forever. Thus, it becomes important to explore the nature of change and the ensuing considerations for policymakers. The changes expected will require a very different kind of labour law that will need to balance the interests of employers and workers.

Labour laws have their origins in the industrial and manufacturing context, where there was a designated workplace, and an identifiable workforce. The laws were primarily focused on addressing power imbalances by mandating recognition of unions, ensuring workplace safety, and creating legal structures for peaceful resolution of disputes. They also allowed for collectivisation of labour to bargain with management for improvement in working conditions.

The next stage entrenched the rights of workers, which were won through collective bargaining. Payment of bonus, gratuity, provident fund, pensions, and health and maternity benefits were enshrined as a matter of right, with a belief that the legal relationship of employee and employer was stable, and capable of determination. However, this notion has been upturned by the rise of gig economy platforms.

The gig economy consists of platforms which connect service providers with consumers. They raise concerns that defy classification in the pre-existing legal frameworks. Companies which own these platforms claim that the service providers are not really workers or employees, but, in fact, "independent contractors", who enjoy flexibility of work hours and freedom to choose nature of work. These "gigs" allow people to step in and out of paid work at their convenience, while also doing away with the requirement of a fixed workplace.

However, workers are always under surveillance with ratings systems, and face threats of deactivation via non-transparent means. Their earnings are also volatile, as far as monthly incomes are concerned. This is specifically disadvantageous to women, who cannot avail of benefits, like maternity leaves available under traditional laws. These concerns co-exist with workplace safety issues. In India, apps such as Urban Clap pose new challenges in terms of safe workplaces.

Countries around the world are waking up to the need for re-orienting their labour laws to address these iniquities. Initial intervention, with drivers and organisations approaching courts, have had mixed results. In the United States, for instance, different state courts took diametrically opposed views on consideration of gig economy workers as employees.

Even courts are limited by the laws and the specific legal frameworks within which they operate.

Besides, court intervention cannot change the fundamental assumptions on which the law has been drafted, namely, a fixed workplace, and an identifiable workforce. While this may matter less in claims concerning minimum wages or social security, such assumptions do matter for occupational safety. Part of the problem lies in defining workplaces since work is carried out at customers' location.

Thus, addressing these concerns requires legislative intervention. A good starting point of such legislative measures will be an acceptance of the changed nature of the employee-employer relationship within the gig economy paradigm. This has to be done with a view to address the serious power imbalances between workers and platforms. Knee-jerk over-regulation might result in a sudden loss of livelihoods, weakening the case for regulations. On the other hand, loose and *laissez-faire* approaches may have little impact on the ground.

> **A good starting point of legislative measures will be an acceptance of the changed nature of the employee-employer relationship within the gig economy paradigm**

At the moment, there are few, if any, coherent legislative proposals at the Union or state level to address these concerns. The government needs to examine existing laws, including the proposed labour codes, and introduce a legislative framework, which will be conducive for gig economy platforms, and the millions engaged in providing their services.

A good starting point can be to address the gaps in the four Codes mooted by the Union government, and proposing legislative tools and policy frameworks that will be necessary to prepare for the coming future.

LETTERS TO THE EDITOR

UK SC ruling

The UK Supreme Court (SC) has shown that it can rule independent of the interest of the government of the day, something judiciaries in other democracies can emulate. Its unanimous ruling that the prorogation of the British Parliament by PM Boris Johnson was 'unlawful'. It was a clinching ruling in that it illumined the nature of Westminster democracy, and made the will of the people, represented by the Parliament, fundamental. It holds out relevance and applicability for our own country as its Parliament is modelled on the British system. The UK top court made it clear that the ruling was about 'prorogation' and not about 'Brexit'. If the ruling vindicated the Opposition's stand on the prorogation of the Parliament and benefited it in the political tussle to get the upper hand, it was only incidental to its establishing the illegality of the prorogation. As a corollary of the ruling, the House of Commons has gavelled into session. The ostensible reason for the prorogation was to facilitate a Queen's Speech 'to outline the new government's new policies and proposals'. But, the real intent was to stymie parliamentary scrutiny. Despite a string of political and legal setbacks, like losing parliamentary majority and receiving court strictures for preventing the Parliament from doing its job, and attracting the charge of stifling democracy, Johnson declared that the ruling with which he 'strongly disagreed' and termed a 'serious mistake' would not deter him from delivering Brexit. There is now considerable uncertainty about Brexit before the deadline. Labour Party's stand is that Johnson has no mandate for a 'no-deal Brexit' and the Brexit crisis can only be settled by a general election.

— G David Milton, Maruthancode

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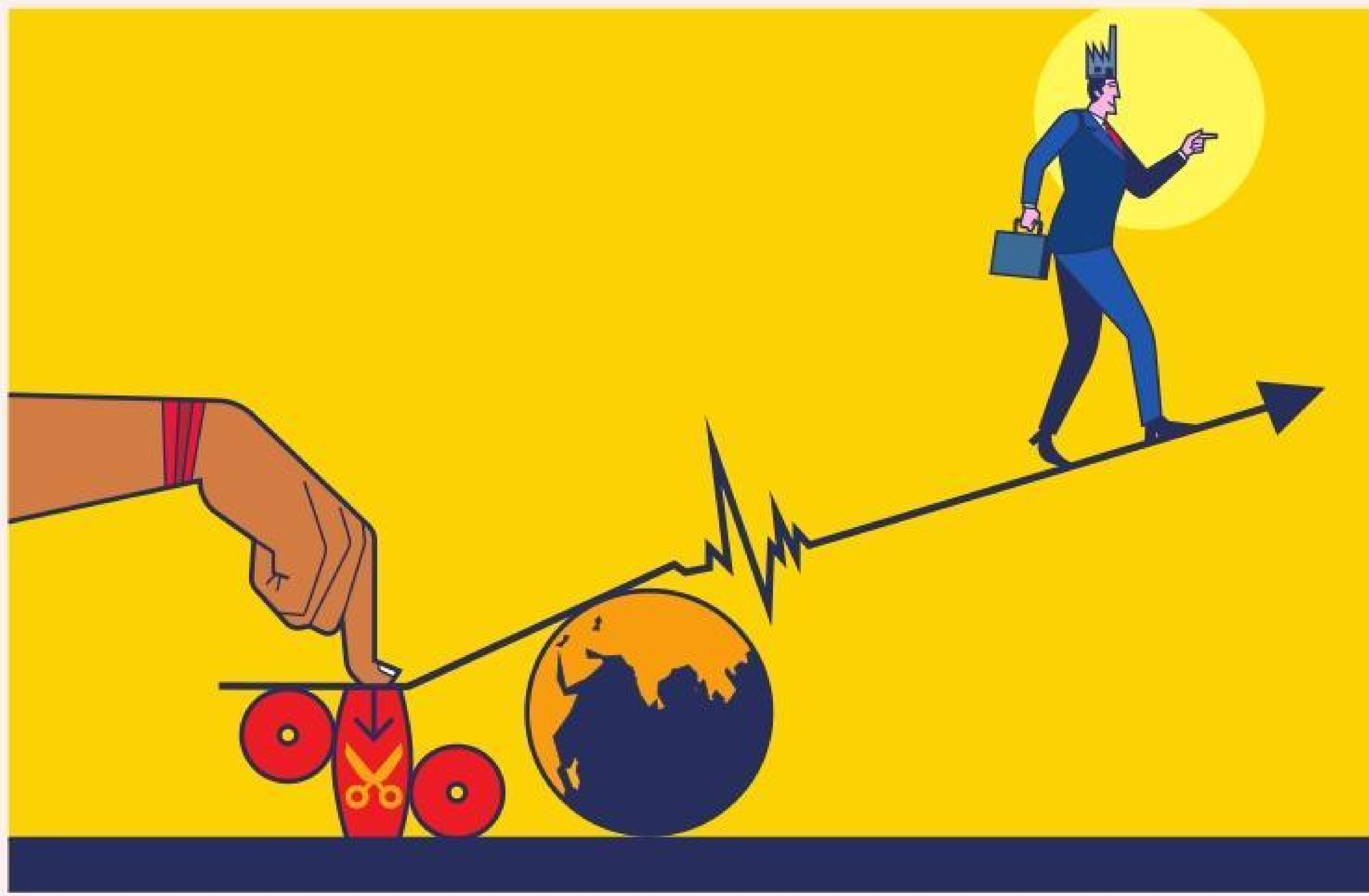

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MODI GOVERNMENT

Incentivising risk-takers, entrepreneurs

Reduced taxes will reduce the pressure on companies to generate higher returns, improve risk-return trade-off for investors, and increase investment

FINANCE MINISTER Nirmala Sitharaman has slashed the corporate income tax (CIT) for domestic companies to 22% in order to promote growth and investment, and announced a new CIT of 15% for new domestic manufacturing companies, thereby providing a boost to the Make-in-India initiative. The new effective CIT would be 25.17% inclusive of a new lower surcharge of 10% and cess of 4%. With this announcement, the Narendra Modi government has fulfilled the promise made by the former finance minister in FY16 of a CIT of 25% with no exemptions/incentives and provided a fillip to manufacturing companies with a lower 15% CIT. It is for the first time that the government of India has used an ordinance to slash IT rates outside the conventional Budget.

India's CIT is now closer to the world-wide average statutory CIT of 23.03%. A study conducted by the Tax Foundation, a tax policy non-profit organisation based in the US, on the CIT rates across 208 tax jurisdictions in 2018 revealed that India had the highest CIT, at 35%, amongst the large economies in the world. The study further indicated that the average statutory CIT rate is 20.65% in Asia, 28.4% in BRICS, 21.86% among EU countries, 23.93% in OECD countries and 27.63% in the G7, which comprises of the seven wealthiest nations in the world. The US has a combined statutory rate of 25.84%. The majority of the 208 separate jurisdictions surveyed have corporate tax rates below 25%, and 103 have tax rates between 20% and 30%.

Before the CIT rate cut, the marginal CIT for FY20 was 35% for companies having a turnover above ₹400 crore in FY18, and dividend distribution tax (DDT) of 20.56%. The accompanying table indicates that these companies had to earn pre-tax income of over 27% in FY20, by investing, running a business and creating jobs to enable investors in that company to earn a post-tax dividend of 12%. After the CIT reduction, it has to earn a pre-tax income of 23.5%, an absolute reduction of 3.5%. A sole proprietor of a business earning more than ₹5 crore in FY20 has to earn only around 21% to get the same return, disincentivising scale! In comparison, a company in the US with an effective CIT of 25.85% has to earn a pre-tax income of 20.22% in CY2019 to enable an investor to earn a post-tax dividend of 12%.

Before the CIT cut, India was collecting a total tax of about 55.64% on the Profit before Tax (PBT), whereas the US collected a total tax of 40.67%. The tax collected by India on PBT increased by 52% between FYs 2013-14 and 2019-20, forcing companies to generate a higher pre-tax income to enable an investor to earn the same post-tax dividend. The compulsion to generate a very high return imposes a high cost on the economy, reduces money for reinvestment, disincentivises investment and makes India a rent-seekers' economy, always intent on avoiding taxes!

The high CIT had increased the cost of capital, thereby making Indian companies globally uncompetitive. Cost of capital is the hurdle rate below which no company would be able to run a sustainable business. The weighted average cost of capital (WACC) in India is around 12% considering 10-year G-Sec rate of 6.5% to 7%, and average risk premium on equity of 5%. The US WACC is 7%, in Europe it is 7.16%, and globally it is 7.9% (Prof Aswath Damodaran, Stern School of Business, NYU).

Indian companies are unable to compete globally when their cost of capital and CIT is significantly higher than the overseas competitors. When overseas companies with a lower cost of capital invest and operate in India, they dominate. In addition, Indian companies become a prime target for acquisition by global companies, which have a lower cost of capital. It is one of the major reasons why our entrepreneurs were selling out their companies, being unable to fight the battle of WACC.

Prime Minister Modi, during his 2019 Independence Day speech, recognised the role and contribution of wealth creators in India. He said, "Wealth creators should not be viewed with suspicion. They are the wealth of the nation. It is necessary that those who create wealth in the country should be equally respected and encouraged." Wealth creators are those who take the risk, invest and create jobs. One big issue deterring the risk-takers was the high taxes on capital in India, which had gone up further in FY20 with the increase in the surcharge for high net-worth individuals (HNI) who are major investors, as well as tax terrorism on an unprecedented scale.

Individuals having an income of more than ₹1 crore are subject to IT surcharge between 15% to 37%, resulting in high tax rates of 35.88% to 42.74%. They pay IT at rates varying between 11.96% to 14.25%, on dividend income exceeding ₹10 lakh and long-term capital gains (LTCG) tax of 12% to 14.25% on gains exceeding ₹1 lakh from listed companies. If the investment is in an unlisted company, the IT is 24% to 28.5%, after considering the indexation benefits. In a listed company, LTCG arises after 12 months, while it is 24 months for unlisted securities, so much for incentivising investment! The risk on unlisted securities is higher due to lack of liquidity and inadequate price discovery, but taxes are more. In India, the higher the risk, higher is the tax. Along with the CIT reduction, the finance minister has also provided some relief to high income earners by withdrawing the enhanced surcharge applicable on capital gains arising on sale of equity shares/units of an equity mutual fund that are liable to Securities Transaction Tax. But the enhanced surcharge on dividend income continues.

Imposition of DDT and the additional tax on individuals on dividend income beyond ₹10 lakh resulted in multiple levels of dividend taxation. Distribution of dividends is another form of return of capital and tax rate on dividends is generally linked to the capital gains tax rate. A higher dividend tax relative to the capital gains tax could discourage companies from distributing earnings through dividends. A reduction in the effective DDT to 15% and withdrawal of taxation of dividends beyond ₹10 lakh will increase the return to investors and incentivise them towards higher investments.

Reduced taxes will reduce the pressure on companies to generate higher returns, improve the risk-return trade-off for investors, and increase investment. Limiting the CIT effective tax rate at 25.17% is enabling Indian companies to provide a risk-adjusted return of 12% to the shareholders at a lower pre-tax income of 23.5% compared to 27% before the rate cut. It will also improve the liquidity for banks and financial institutions for lending and enable them to reduce lending rates. This should increase the capital efficiency of the economy and provide the much-needed growth impetus for the economy.

Pre-tax return required to generate 12% post-tax income

	FY19-20[1]	FY19-20[2]	FY13-14	US CY19
Equity investment (₹ cr)	100	100	100	100
Profit before tax (₹ cr) (A)	23.52	27.05	21.90	20.22
Pre-tax return on equity (%) (derived figure to get to after tax ROE of 12%)[3]	23.52	27.05	21.90	20.22
Corporate tax rate (%) (B)	25.17	34.94	33.99	25.84
Corporate tax paid (₹ crore) (C = A * B)	5.92	9.45	7.44	5.22
Profit after tax (₹ crore) (D = A - C)	17.60	17.60	14.46	15.00
Dividend distribution tax rate (%) (E)	20.56	20.56	17.00	0.00
Dividend distribution tax paid (₹ cr) (F = D * E)	3.62	3.62	2.46	0.00
Dividend paid to shareholders (₹ cr) (G = D - F)	13.98	13.98	12.00	15.00
Dividend tax - high net worth individual (%) (H)	14.25	14.25	0.00	20.00
Dividend tax paid by HNI (₹ cr) (I = G * H)[4]	1.98	1.98	0.00	3.00
Net return (dividends) to shareholders (₹ cr) (J = G - I)	12.00	12.00	12.00	12.00
Total tax to govt. (₹ cr) (K = C + F + I)	11.52	15.05	9.90	8.22
Total tax to govt. (% to PBT) (L = K/A)	48.98%	55.64%	45.21%	40.65%

Note:
(1) After the CIT rate cut on 20th September 2019. CIT @ 22%; surcharge @ 10% and Health and education cess at 4%. Effective tax rate (ETR) is 25.17%; (2) Before the CIT rate cut. CIT @30%; surcharge @ 12% and Health and education cess at 4%. ETR is 34.94%; (3) A net return of 12% to shareholders is considered by summing up the government of India bond rate of 6.5% to 7% and an average risk premium on equity of 5%; (4) It is assumed that an individual having a total annual income of more than ₹5 crore has invested in a private company and the entire dividend received is more than ₹10 lakh.

CORPORATE TAX CUT

A bold move by the government

VISHAL ANAND

The author is partner, Corporate & International Tax, PwC India

With reduced tax rates for domestic companies, India will be on a par with the global economy

WITH THE APPROACHING festive season, corporates and investors have been given an early present as finance minister Nirmala Sitharaman has proposed certain tax rate reductions and other relief aimed at boosting the economy and promoting growth and investment. These proposals will be brought in through the Taxation Laws (Amendment) Ordinance 2019 that will make certain amendments to the Income-tax Act 1961 (Act) and the Finance (No. 2) Act 2019. These amendments are mainly in relation to reduction of income-tax rates for domestic companies. The key features are:

Headline tax rates for domestic companies reduced to 22%: A new provision will be inserted into the Act (Section 115BAA), providing a domestic company with an option to pay income-tax at the rate of 22% (plus applicable surcharge and cess), subject to condition that while computing total income, they will not avail any exemption/incentive such as deduction under Section 10AA, accelerated depreciation, additional depreciation, investment allowance, deduction of capital expenditure on specified business and expenditure on scientific research or claimed any set-off any brought-forward losses attributable to such deductions, etc.

This amendment has been aimed at promoting growth and investment and will come into effect from assessment year (AY) 2020-21 onwards. The option is required to be exercised on or before the return filing due date, and once the option is exercised, it cannot subsequently be withdrawn. Further, domestic companies opting for such concessional tax regime will not be required to pay the minimum alternate tax (MAT). The tax rate for companies opting for this regime is to be increased with a surcharge of 10% regardless of the quantum of income.

For domestic companies that decide not to opt in for this concessional tax regime and continue to claim tax holiday/incentives will continue to pay income-tax at the prevailing rate of 25%/30% (plus applicable surcharge and cess), depending on the turnover threshold of ₹400 crore for FY18. However, the headline MAT rate has been reduced from 18.5% to 15% with effect from AY2020-21. Such companies can also opt in for the concessional tax regime after the expiry of tax holiday/exemption period.

Reduced tax rate of 15% to domestic manufacturing companies: To provide a boost to the 'Make in India' initiative and attract fresh investments in manufacturing, a new provision is proposed to be introduced (Section 115BAB) to provide an option to a newly incorporated domestic manufacturing company to pay tax at a rate of 15% (plus applicable surcharge and cess). This option is available to a domestic company subject to the following conditions:

- It is incorporated on or after October 1, 2019, and commences its production on or before March 31, 2023, and (i) is not be formed by splitting up/reconstruction of business already in existence, (ii) does not use any previously used machinery or plant, and (iii) does not use any building that was previously used as a hotel or a convention centre;
- It is engaged solely in the business of manufacture or production of an article or thing and research in relation to, or distribution of, such article or thing manufactured or produced by it; and
- While computing its total income, it has not availed any exemption/incentives such as deduction under Section 10AA, accelerated depreciation, additional depreciation, investment allowance, deduction of capital expenditure on specified business and expenditure on scientific research or claimed any set-off any brought-forward losses attributable to such deductions, etc.

The above option is required to be exercised on or before the return filing due date, and once the option is exercised, it cannot subsequently be withdrawn. Domestic companies opting to be taxed under this regime will not be required to pay MAT. Similar to above, the tax rate for companies opting for this regime is to be increased with a surcharge of 10% regardless of the quantum of income.

With the reduced tax rates for domestic companies, India will now be on a par with the global economy. Manufacturing sector is likely to get a boost with the headline tax rate for newly incorporated domestic manufacturing companies being reduced to 15%. The proposed measures and amendments will provide a fillip for both domestic and foreign investments, which will provide a boost to India's economy.

Turning farming into enterprise

The only way the farming sector can be brought back from the 'take home' to 'reap the value' model is through collectivisation of farmers' interests through FPOs

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INDIAN AGRICULTURE SECTOR, despite the sharp reduction in its contribution to GDP from 58% in the 1950s to 18% in 2010s, continues to support the livelihood for half of country's population. The dependence of the population on agriculture has resulted in fragmentation of farm holdings, not only rendering them uneconomical, but has also put them on weaker pedestal in terms of bargaining power. The average farm size in India stands much smaller at about 1.3ha, against 169ha in the US, 53ha in the UK, 52ha in France and 45.7ha in Germany. The fact that 86% of total operational holdings in the country are of small and marginal farms (size less than 2ha, Economic Survey 2019) indicates the reasons for the perpetual indebtedness and low incomes in Indian farming. A World Bank report (2019) on Maharashtra Agricultural Competitiveness Project, conducted during 2011-18 to increase productivity, profitability and market access of the farming community in the state, suggests that aggregated marketing through FPOs increased profitability to about 45%. Besides enhancing bargaining power, FPOs bring the advantage of economies of scale in both pre- and post-harvest farm operations, enhancing profit margins, and can also establish forward- and backward-linkages that can bring back the value of services such as warehousing, quality standardisation, finance, etc, from the existing opaque, dilapidated and inefficient value chains for most agricultural commodities.

Collective operations in Indian agriculture have a century-old history, with the enactment of the Cooperative Society Act 1904 that enabled formation of agricultural credit cooperatives. The momentum in formation of FPOs gained following the amendment to the Companies Act 1956 in 2002. Among the 5,000 FPOs registered in India during the past decade and a half, about 3,200 are registered as FPCs, while the rest as cooperative societies (NABARD 2018). NABARD and the Small Farmers' Agri-Business Consortium (SFAC) are actively promoting FPOs, apart from state governments and other Indian and international funding agencies.

Despite efforts to promote FPOs, the progress has been limited primarily due to operational and structural issues. Most operational constraints are due to lack of adequate financial resources and infrastructure facilities, inability to establish forward- and backward-linkages, lack of skills and professional expertise, inadequate awareness amongst farmers as well as financial institutions about FPOs, etc.

Inadequate finance, indicated by many field studies, turns out to be the single largest impediment for success of FPOs. Though the Equity Grant and Credit Guarantee Fund Scheme under SFAC covers FPCs with a minimum membership of 500 farmers, those FPOs and FPCs with smaller memberships would be deprived. Interest rate subvention, similar to that provided to crop loans, should be provided to reduce the cost of financing to all FPOs\FPCs.

A prerequisite for the success of FPOs is adequate access to regulated warehousing so they can store their produce till they get remunerative prices, while meeting their immediate financial requirements by connecting to the institutional financial system through warehouse receipts. At present, warehousing capacity is estimated at 158.5 million metric tonnes (mmt), significantly lower than the required capacity of 252 mmt (at 80% of 315 mmt) of foodgrains and oilseeds produced annually in the country. Regulated warehouses within the existing warehousing capacity are much smaller at about 8 mmt.

A concern area is lack of awareness amongst farmers and inadequate infrastructure facilities for meeting required quality and standards of agricultural produce so that their farm produce can fetch a better price. At present, most of the crop output is sold to traders without even grading and standardisation due to lack of facilities and awareness amongst farmers, leading to less price realisation. In this regard, the World Bank report (2019) indicates that simple adoption of sorting and grading practices had increased farm profits by 15% on an average. In addition to creation of infrastructure for quality standardisation and grading, awareness of the same and its benefits such as better price realisation for their produce and access will help them adopt techniques and practices whose adoption will help them produce to market expectations.

Skill development is another area that needs to be addressed. Majority of the existing FPOs have been involved in the areas of aggregation for marketing and sales, followed by input procurement and to some extent processing. In this regard, it is essential to ensure there are adequate facilities for skill development in FPOs to take the farmers' produce through various stages of supply chain. In addition, adequate facilities shall be provided to impart entrepreneurial skills amongst farmers, particularly officiating members, so that FPOs can be managed professionally.

The distribution of FPOs is skewed to seven states (Tamil Nadu, Karnataka, Madhya Pradesh, West Bengal, Maharashtra, Rajasthan)—50% of total FPOs in India. Appropriate awareness around FPOs, their formation process and their demonstrated benefits must be spread amongst farmers of states with lower penetration.

Apart from operational issues, we need to address structural problems through consolidation of the ecosystem within which modern-day FPOs operate in.

Recent success stories show that FPOs can be the ultimate model for increasing farmers' incomes and empowering them through collective operation and better bargaining power to gain larger share in consumer price. One such success story is Nashik-based FPC Sahyadri Farms, set up in 2011, which has grown to be the largest FPO in India with 8,000 farmer members and having a turnover of ₹3,000 crore.

The only way the farming sector can be brought back from the 'take home' to 'reap the value' model is through collectivisation of farmers' interests through FPOs, and what better it can be if a statutory authority provides for their enhanced presence, connecting them to financial sources and institutions, and the ability to move them up the value chain.