Opinion

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COUNTER STRIKE

Chief of defence staff, General Bipin Rawat

"As long as there are states which sponsor terrorism, we will have to live with the menace. We need to take the bull by its horns and strike at the root cause. If we think the war on terrorism is going to end, we are wrong"

RationalExpectations

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Govt biggest loser when Voda Idea shuts

It owes govt over ₹215,000 cr & banks ₹50,000 cr; if a Vodafone Idea shuts after investing \$50+bn, this will scare others too

APART FROM INVESTORS in both Vodafone Plc and Idea Cellular, the Government of India will be the biggest loser if Vodafone Idea shuts down, as looks increasingly likely, with the Supreme Court refusing to review its faulty ruling on the AGR dues of the telecom industry; apart from anything else, the fact that a PSU (Gail) which earned ₹35 crore in revenues needs to pay ₹172,656 crore of AGR dues should make it clear how faulty the judgment was. While Vodafone Plc invested around \$30 bn in its India operations — Idea invested around \$21 bn — and will lose all of this now, the government stands to lose ₹53,000 crore in AGR dues, ₹5,700 crore in one-time-spectrum-charge (OTSC) dues, and another ₹157,750 crore of deferred payments for spectrum that Vodafone Idea bought in the past. In addition, banks are owed around ₹49,000 crore, and it is not clear how much of this is secured by assets, or how much banks will get once the company goes to the insolvency courts.

Theoretically, the government will lose only the AGR and OTSC dues since it can take back its spectrum once Vodafone Idea fails to pay and then re-auction this. Apart from it not being clear whether this can be done without going through the legal process, even if it can, it is unlikely the government will be able to resell the spectrum for anywhere near the same amount. For one, with the glory days of telecom behind us, the government's revenues fell from ₹70,241 crore in FY17 to ₹39,345 crore in FY19 as there were no auctions in 2017, 2018, or 2019; and, with just two players left in the industry, the competitive intensity for auctions will also be much lower in the future.

If investors buy the government's argument of commercial failure being an inherent risk in any business, the collapse of Vodafone Idea may not affect either local or foreign investors, though a telco with 336 million customers folding up would frighten most; more so, given the \$50+bn investment by Vodafone and Idea. If, however, as is likely, investors focus on the government inaction, and unfriendly policy, that led to this state of affairs, the impact will be even higher—and this at a time when investment levels in the country have been falling for several years anyway.

AGR dues, ₹ crore

Private sector	
Bharti Airtel	43,318
Vodafone-Idea	49,155
Public sector	
Power Grid	22,062
Gail	1,72,656
Delhi Metro	5,482
RailTel	307
STPI*	90

*Software Technology Parks of India

The AGR dues are essentially dues of licence fee (LF) and spectrum usage charges (SUC); so, if LF/SUC had been scrapped, the AGR dues would be much smaller than they are today. The question, then, is why LF/SUC should have been scrapped. In the past, India virtually gave away the spectrum free—there was an auction for the initial spectrum, but the bulk was not charged for—and so, in return, the government charged telcos an LF/SUC as a share of their revenues. In 2010, however, following the A Raja scam and the SC cancelling the licences he gave, spectrum was auctioned and, thanks to this being done in a faulty manner, telcos paid an arm and a leg for this. To use a parallel from the housing market, why should buyers be paying hefty EMIs when they have already paid the cost of the flat upfront? Ideally, this decision should have been taken by the Manmohan Singh government in 2010, but the Modi one elected in 2014 did nothing either.

It gets worse. The SC verdict was incorrect because, till then, there was no clear court verdict on AGR; indeed, AGR demands by the government were set aside by various courts in 2006, 2007, 2011, and 2015. So, if the SC verdict was the final one on what constituted AGR, there should have been penalties and interest levied upon the basic AGR dues. The SC erred on this count, and on others too since the issue of what comprised AGR was never really examined by any neutral tribunal like the TDSAT before. But despite this, the government didn't even appeal on the penalties etc. Over 75% of the AGR dues of telecom players are on account of penalty, interest, and interest upon interest.

Indeed, even after the AGR ruling, the government had the option of scrapping LF/SUC which, given the haemorrhaging in the sector, should have been done anyway. It would have saved the telcos and, equally important, safeguarded government revenues. With LF/SUC scrapped, telcos would have found it easier to raise money to pay the AGR dues. But, as in the past, the *suit-boot-ki-sarkaar* fear paralysed the government.

Contrast this with what the Vajpayee government did when faced with a similar situation, where telcos were defaulting on tens of thousands of crore of licence fee dues. It came up with NTP 1999, which converted the licence fee to a revenue-share one and, as part of the deal, it ensured that many telcos could be allowed; till 1999, just two telcos were allowed in each telecom circle. This ensured the industry boomed and, within a few years, the government had more than made up the licence fee it had foregone.

Postscript: While many believe the ₹2 lakh crore owed by PSUs is just a paper entry—one arm of government paying another—even if this is reinjected into the PSUs later by way of fresh equity, they will have to raise the money within a week. This means either raising it from banks or from bond issues; both will take time, and neither will be easy.

Expect fall in UPI volumes

If govt doesn't reverse MDR order, can hit FDI flows also

THOUGH THE GOVERNMENT stopped commissions—Merchant Discount Rate, or MDR in jargon—on all UPI payments as well as RuPay cards from the beginning of the year, in the belief that more merchants would start accepting UPI payments once the MDR was abolished, this is premised on incorrect assumptions. While the MDR used range from 0.25% to 0.65% (for transactions above ₹2,000), this is now a flat 0.3%. Indeed, thanks to the way UPI commissions are structured, 80-85% of the 5-6 million merchants who accept UPI payments do not even pay MDRs. This is because there is no MDR on transactions below ₹100 and, thanks to a category called UPI P2PM created two years ago, no MDR charges are paid by merchants who have a monthly turnover of ₹100,000; this used to be ₹50,000 earlier. If firms like PhonePe, PayTM and Google were spending money to get merchants to use their UPI-based services despite this, it was because they hoped that, over time, the merchants would get bigger and start paying MDR.

If fintechs like PhonePe or PayTM can no longer make money through MDR, and there are going to be more restrictions on how consumer data can be used, the government has to ask itself why fintechs, or banks, will invest in promoting UPI or RuPay cards. In which case, this can affect FDI flows into fintech, estimated at \$2.5 bn last year, as well. Sure, a government mandate may force more firms to offer their customers UPI/RuPay services, but offering this and encouraging customers to use them are two different things; in any case, the mandatory on-boarding applies to firms that have an annual turnover of more than ₹50 crore, and so, does not apply to the majority of merchant outlets in the country. Whether the government can force PSU banks to push RUPay, if the banks incur more costs than they earn from getting merchants to use their cards, is not certain.

Another issue the government needs to think about is whether it was MDR commissions or something else that was slowing merchant acceptance of UPI/digital payments. Given most merchants don't pay MDR anyway, chances are merchants are more afraid that accepting payments via UPI will put them into the tax net as all payments will be routed to their bank accounts. Apart from what this does in terms of their tax liability, they can also come under the scrutiny of other government agencies like EPFO etc. Unless the government reverses its order, one of its biggest achievements in terms of digitising payments can start coming undone.

GROWTH STRATEGY

INDIA'S PAST DOES NOT INSPIRE CONFIDENCE. IF THE TOT MODEL FAILS AND INSOLVENCY CREEPS INTO NHAI, PFC, ETC, INDIA COULD BE STARING AT A LOW-LEVEL GROWTH TRAP

Getting real on infra-led growth

RENU KOHLI
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Views are personal

EVER SINCE THE success of the Golden Quadrilateral National Highway Project, initiated by the Vajpayee government in 2001, investment in ambitious infrastructure projects has caught the imagination of policymakers. Various public policy documents have tried to quantify such ambitions into investment targets: The 11th five-year plan (FY08-12) under the UPA government was able to raise infrastructure investment to 7% of GDP—a target advocated by the World Bank's *Growth Report*, 2008. Emboldened, it set an even higher target of 8.2% in the 12th five-year plan (FY13-17), but the bang ended in a whimper, a mere 5.8% of GDP. The ₹102.5 lakh crore infrastructure spending plan under National Infrastructure Pipeline (NIP) is another attempt to scale up the ambition—albeit to kick-start sagging economic growth!

Thus, big infrastructure spending is back, centrestage of a growth-revival strategy when private domestic demand has collapsed. This has certainly excited its advocates. But, critics have questioned the government's capacity to mobilise funds given on- and off-budget fiscal limitations. Whether the government should cross the fiscal red line has become contentious: With general government debt at 70% of GDP, it must be worrying about the market appetite for more borrowings and patience of credit rating agencies. Having let current expenditure expand both on and outside the budget over the last six years, the Modi government has only itself to blame for not having the space to invest in infrastructure.

There is no disagreement the country has a huge infrastructure gap, as is well articulated in the NIP report. The real challenge is to find resources. "Money does not grow on trees" is an old saying. By now, the government should have internalised that forced filing of more income tax-GST returns does not automatically guarantee higher tax buoyancy. So, the way forward appears to be to borrow and invest. Whether these would be on/off-budget are matters of detail. Notwithstanding the emerging financing challenge, this article intends to bring some stylised facts and a sobering account of India's past experiences of infrastructure investment-led growth, both for the government and the private sector.

Historically, the larger share of infrastructure investments has come from the central and state governments (see graphic). In the 10th five-year plan (FY02-07), this was a modest 5% of GDP and appropriately funded; one could argue, this was likely demand-led, or at least so enabled, as genuine fiscal consolidation happened in the period. The 2008 crisis, and the resulting sharp dip in GDP growth led UPA II to reorient its growth strategy and put infrastructure investment at the core plan for economic revival.

As G20 consensus to let countries with fiscal room spend evolved, government investments were scaled up in the 11th five-year plan; the fiscal deficit more than doubled in the two years to FY10. More importantly, the private sector was roped in with supportive policy incentives, and bank financing. Private enthusiasm is evidenced by the fact that India was the top receiver of PPI activity (Private Participation in Infrastructure, World Bank) between FY08-12, accounted for almost half of new PPI investments in developing countries in 2011; its public-private partnerships (PPPs), too, are one of world's largest programs. Several warnings that banks could face asset-liability mismatch were simply bypassed!

Growth recovery was short-lived and ended abruptly as the booster turned out to be artificial, and unsustainable. As macroeconomic conditions deteriorated, most of these investments turned bad. The outcome was near-complete economic paralysis: The government was forced to tighten its belt; overleveraged corporates were left with impaired and weakened balance sheets, and the banks saddled with NPAs. The collateral damage, however, radiated much beyond these as motives were ascribed to many of these investments. Instead of critically questioning the growth-revival strategy through ambitious infra-investment targets, the blame was heaped on entrepreneurs and bankers. The fallout was that the private sector withdrew from infrastructure altogether, and banks became completely risk-averse.

However, fascination for investing in big infrastructure projects continued under Modi 1.0. The excuse was to deploy public investment in infrastructure as a countercyclical tool. Ambitious road and railway projects were rolled out, financed largely through off-budget spending, quasi-government guarantees extended to government-owned National Highways Authority of India (NHAI), Indian Railway Finance Corporation (IRFC), etc. In spite of the breathtaking pace at which roads and railtracks were built in these last five years, the growth outcome has been no different. Some private NBFCs enticed into fresh infrastructure exposure ended up damaging their balance sheets, just as banks did under UPA-II. The government's tagline that it would monetise assets built under EPC contracts through toll-operate-transfer (TOT) model has hardly any takers.

The medium-term impact of infrastructure investment-led growth experience can, thus, be summarised in the following stylised observations:

- Elevated non-performing assets (NPAs), risk-aversion of banks to infrastructure exposure, lending standstill, partial response to monetary policy changes;
- Shrinkage of private interest and equity participation in infrastructure;
- Fiscal deterioration, crowding-out, high interest rates, with low inflation and monetary easing;
- Further deceleration of growth extending to consumption slowdown, non-restoration of private investment;
- More importantly, efficiency gains, though visible, could not yield the desired competitive edge, e.g., corporate savings are decelerating since FY14.

It is time to critically question the strategy to revive growth through ambitious infra-investment targets much beyond the economy's financing capacity. It was the World Bank's *Growth Report* (2008) that suggested countries aiming to grow faster should invest 5-7% of GDP in infrastructure; this, at best, was a historically-observed statistical correlate. But, India's experience, so far, has been to the contrary. It is, instead, a glaring example of how scaling-up infrastructure investment has failed to uplift growth and crowd-in private investment, caused serious collateral damages to the critical business and financial sectors, worsened public finances, and clogged macroeconomic channels.

Whether India is able to sustainably finance more than 7% investment in infrastructure remains an open question! The National Infrastructure Pipeline (NIP) rolled out by Modi 2.0 is another ambitious plan on the table, ostensibly to achieve a \$5-trillion economy. The narrative sounds familiar—should we worry?

Given the lack of private appetite, NIP conceives public sector to finance 78% of the planned ₹102 lakh crore of investments. Of this, nearly 60% of the central government share is off-budget financing (see graphic). Effectively, this would perpetuate diverting of most financial surpluses towards the government sector, be this through banks, bonds, or any other method.

But, more emphatically, one should not forget how such ambition has impacted the country's private sector, banks (both public and private), and NBFCs in the past. What has survived so far are government-owned, mega institutions, such as NHAI, PFC, IRFC, etc, which are mostly backed by quasi-sovereign guarantee or the status in fund raising. One should worry if the TOT model fails to achieve significant monetisation of public assets, and insolvency creeps into these institutions too, because few missteps, and India could be staring at a low-level growth trap in the decades ahead! Tread with caution.

India: Infrastructure investments, amount and composition

	Year	Total investment in infrastructure % GDP	Total investment in infrastructure (₹ lakh cr)	Public % GDP	Public (₹ lakh cr)	Private (₹ lakh cr)	Private % total
10th plan	2002-07	5.02					
11th plan, Actuals	2007-12	7.02	23.8	4.82	14.9	8.9	37.4
12th plan, intial proj	2012-17	8.18	55.7	4.53	28.9	26.8	48.1
12th Plan, rev proj	2012-17	5.73*	36.0	3.89	24.4	12.8	35.6
Shortfall			19.7		4.5	14.0	12.6
	2017-18	5.97	10.2	3.88	6.63	2.50	24.5
	2018-19	5.26	10.0	3.42	6.50	2.50	25.0

Sources: 11th-12th Plans - Appraisal document of Twelfth five-year plan, 2012-17, pg 179
FY18, FY19 - National Infrastructure Plan, DEA, 2019, pg 20 with author's calculations *(proj. 5.84)

Central govt financing of NIP

₹ lakh cr	FY19(RE)	FY20(BE)	FY21(P)	FY22(P)	FY23(P)	FY24(P)	FY25(P)
A Total capital outlay by Centre (infra)	3.54	3.77	4.58	5.56	6.76	8.21	9.97
B Budgetary support (infra)	1.39	1.53	1.86	2.25	2.74	3.33	4.04
C = B/A (%)	**39**	**41**	**41**	**41**	**41**	**41**	**41**
D=B/E (%)	**0.73**	**0.74**	**0.82**	**0.89**	**0.96**	**1.03**	**1.11**
Incremental budgetary support/GDP vs FY20 (%)			0.07	0.14	0.21	0.29	0.36
E GDP in ₹ lakh crore	190.1	205.37	227	254.27	286.42	323.25	365.49
% total NIP exp							
Centre total outlay		27.6	23.5	29.3	49.0	64.2	90.2
Budgetary support		11.2	9.5	11.9	19.9	26.1	36.5
Extra-budgetary resources		16.4	13.9	17.5	29.1	38.2	53.6
in ₹ lakh cr **[A-B]**		**2.24**	**2.72**	**3.31**	**4.02**	**4.88**	**5.93**

Source: Report of the Task Force, Department of economic affairs, ministry of finance, Government of India, pg 89

Reviving the real estate sector

From increasing the CLSS income caps to reducing GST on cement, there are quite a few moves the government should consider

RAJANI SINHA
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REAL ESTATE IN India faces a severe credit crunch. The sector depended heavily on NBFCs for its credit requirements. Hence, the sharp slowdown in NBFC sector and NPAs plaguing the banking sector has had severe repercussions. RBI's latest Financial Stability Report highlights that overall credit (Bank + NBFC + HFCs) to the sector grew by 21% y-o-y in June 2019, against 37% the previous year. Yet, small developers are feeling the credit squeeze—the share of NBFC in credit availability to the sector has gone down. Access to credit at a lower cost would be a big relief for the sector. The government should give the sector 'industry' status to help it access funds at lower rates and cut down cost of capital. The Centre's Alternative Investment Fund, for last-mile funding of affordable housing, is also in the right direction. But there is urgent need for quick and effective implementation.

The other big challenge is dwindling demand. Private final consumption expenditure has been recording weak growth, reflected in poor sales growth of even FMCGs. With the consumer pessimistic, housing, a high-ticket consumption item, has been severely impacted. At present, Section 80C of the Income Tax Act does not provide for a focussed benefit on housing. A separate annual deduction of ₹150,000 for principal repayment will provide the much-needed fillip for home loans. A segment that specifically requires further government's attention is the Affordable Housing. Despite budget efforts, conversion of latent demand to actual sales has been slow. Even while affordable housing launches have been strong, sales have fallen by 8% in 2019 (lower-than ₹50 lakh price segment in the top-8 cities). The annual household income cap for availing the Credit Linked Subsidy Scheme benefits should be increased across all categories so that it is in sync with house prices in major urban markets. The affordable housing price definition should also be increased from ₹45 lakh (considering house prices in major markets) to enable lower GST rate benefits to a wider consumer base. Moreover, reducing the cement GST from 28% will provide a big fillip to infrastructure and housing sector.

A positive development is that now, demand is mainly from end-users. Of the total demand, only 5-10% is from investors, against 60% investor participation seen in cities like Mumbai and Delhi in the past. This has helped reduce artificial escalation in prices. It is better to encourage investors' appetite for real estate sector through REIT (currently available in the commercial real estate space). The one REIT listing we have had so far has given attractive returns and there are more REITs lined up. The government should make investment in REIT attractive by reducing the timelines of investment from three years to one year for long-term capital gains taxation.

Taking the real estate sector out of the woods is critical due to its strong linkages with other sectors. Of foremost concern is the high exposure of the banking and NBFC sectors to the real estate sector. Banks' exposure to the real estate sector is around 21% of total loans and advances while that of NBFCs is around 6% of the total assets. Hence, a stress in the real estate sector has its repercussion on the banking and NBFC sector in the form of higher NPAs. On the other hand, a pick-up in demand in the real estate sector can boost overall demand and employment growth.

LETTERS TO THE EDITOR

On housing loans

Apropos of "Delinquency rates in housing loans, credit cards rise in Sept quarter," January 16, in the noteworthy backdrop of housing for all, it is imperative that the momentum of mortgages continues without any constraint. Most importantly, housing for everyone is a prime mover and a much needed necessity. Banks and lenders have been making all efforts under all housing schemes including Pradhan Mantri Awas Yojana (PMAY). In the wake of creeping delinquency rates, it would be worthwhile if CIBIL melas are arranged along with housing loan roadshows. Finances are built on income, expenses, creating assets and repaying back liabilities. Asset creation, like home effects, rest three blocks of finances. It has to be explained to the borrower of a house loan, and make house owners understand that expenses will have to be reined in or income has to be raised to account for asset creation that is home. It is necessary to impart importance of CIBIL to all credit card and borrowers of buying a house.

— NK Bakshi, Vadodara

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GOODS AND SERVICES TAX

In pursuit of reforms

Can India focus on reforms by states instead of being obsessed with GST Compensation?

FOR THE FIRST time since July 2017 the finance ministry has released state-wise data of GST collections for December 2019 and 2018. Out of ₹80,849 crore collected, shares of Maharashtra are 20.4%, Karnataka 8.5%, Gujarat 8.2%, Tamil Nadu 7.9%, Uttar Pradesh 6.8%, West Bengal 4.6%, Kerala 2% and Punjab 1.6%.

Can the finance ministry release state-wise cumulative numbers for April to December 2019 and thereafter release such numbers monthly? On the issue of compensation, we must know that "according to the GST Compensation Act, states will receive GST compensation in case actual SGST collections fall short of projections. The projection of SGST revenue is based on annual growth rate of 14% with reference to net collection subsumed under GST in 2015-16."

AK Bhattacharya has highlighted that "14 states projected an SGST revenue growth between 14-27% even though economic growth had already begun decelerating." Further, states complaining the most about delay in receipt of compensation had projected high SGST collection growth rates. Kerala, for instance, had projected a rate of 26%, Rajasthan had fixed 23% and Madhya Pradesh had estimated 20%, unlike Maharashtra and Gujarat, which projected about a reasonable 14% growth in revenues. *(Business Standard, Jan 2)*

Can state finance ministers give reasons for over-optimistic revenue projections? Is administration of GST and economic growth only the responsibility of the central government?

We are a strange country! While governments are obsessed with increasing revenue, there are hardly any discussions about reducing government expenditure. Does the government realise that imposing a special coal cess, renamed 'GST compensation cess', increases fuel cost and impacts competitiveness of India Inc?

Further, there is so much focus on the work of the central government, when the country is largely run by the states.

So, then why is the national discourse not focused on states? For instance, there is a need to assess why the situation on state-wise aggregate technical and commercial losses under Ujjwal DISCOM Assurance Yojana. Have states hiked electricity rates as promised under UDAY?

How many states have scrapped the APMC (Agricultural Produce Market Committees) Act and started farmers markets (where farmers sell directly to consumers) in urban centres as Mumbai has. What are mandi tax rates levied on agricultural produce? What is the percentage of land under irrigation and per year increase?

Also, which states have not implemented RERA (The Real Estate (Regulation and Development) Act? Why are builders not being asked if they have reduced prices substantially to stimulate demand? All that we are told is that the real estate sector is down, adversely affecting employment and growth.

Do we not realise that if the states alleviated farmer duress, the Centre would not need to introduce schemes like 'Farmer Income Support' (₹6,000 per annum)

Importantly, no one speaks about the pressures on the financial and administrative capacity of the Indian State because of a burgeoning population and impact on fiscal deficit because of a more than 100% increase in subsidy owing to Right to Food Act.

States can learn from companies in this regard. Governments should have sessions where companies like Hindustan Unilever (Disclosure: I worked for Hindustan Lever), with a turnover of ₹39,310 crore, can organise a training program for state finance ministers and chief secretaries showcasing its relentless focus on cost control? (Disclosure: I worked with Hindustan Lever Limited). Money saved is money earned. Right!

Another learning from well-managed companies is to use profits made during good times to sail through a downturn. Conversely, for the government it means reduce fiscal deficit when growth rates are high and increase deficit when growth falls.

We must appreciate the good work in GST implementation because removal of check-posts and barricades from the state borders have reduced travel time substantially. According to Raghu Dayal, "Crisil found that implementation of GST in the logistics industry would reduce logistics costs up to 30% over 3-4 years." *(FE, Jan 1)*

Let us return to the issue of GST compensation to states and what happens after the five year assured return ends in June 2022. At the outset, it must be stated that a 14% assured growth in revenue collection under GST, on a 2015-16 base, is untenable. When the average annual growth rate in VAT, entry tax, and central sales tax (excludes taxes collected by local government and authorities) for 2012-2016 had a range of 3.8 to 12.6%, and exceeded 14% only for Bihar, is the 14% rate justified?

If the states still feel that it is indeed, can they place in public domain average growth rate of taxes subsumed under GST for ten years prior to its introduction.

Also, why should all states have a common assured return percentage? Moreover, when anything is guaranteed it invariably results in sub-optimal performance and states with better tax-efficiency are penalised.

Given the shortfall, there are concerns, regarding the impact of withdrawal of GST compensation beyond June 2022 on India's fiscal management and, therefore, macroeconomic stability. There are suggestions that the matter needs to be referred to the 15th Finance Commission, even though it does not fall within its purview.

Since states had given away the right to impose levies, and have limited taxation power, a compensation is certainly desirable.

Before looking at a new way to pay compensation it is worth comparing monthly revenue under protection (RUP) state-wise for 2022-2023 (NIPFP) with state-wise gross GST collected in December 2019.

The comparison shows that Andhra Pradesh, Bihar, Kerala, Madhya Pradesh, Rajasthan, Uttar Pradesh and Punjab are where revenue projections are significantly higher than December 2019 actual revenues.

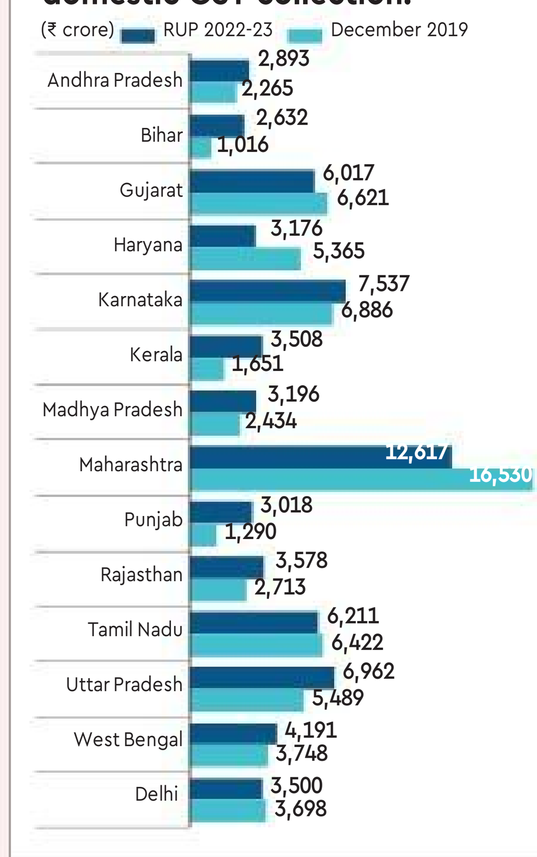
Can chief ministers pro-actively present a plan on how they will increase economic growth rates and GST revenues? A new way of paying compensation to states could be a debt-equity model that provides a minimum increase and an incentive to tax-efficient states.

Just like a debt instrument provides an assured return, all states should be provided an assured increase in revenue growth, say, 6%. Whilst capping the maximum compensation payable to states at say 9%, the difference of 3% would be given to states based on national nominal GDP growth and increase in state GST revenues. The Centre must make this process fully transparent.

Compensation would be funded through a cess as is done presently. Any unutilised balance in the GSTCC in a given year would be transferred ONLY to states in a pre-determined ratio. However, surplus of one year would be adjusted against the compensation payable in the immediate next year. It would not be mandatory for the Centre to fund the cess shortfall.

Hope this addresses state concerns. If states focus on reforms, cost-control, tax-efficiency, non-GST sources of revenue and sell unprofitable public sector undertakings the uncertainty arising from change in compensation mechanism can be managed.

Unfortunately, we as people of India are good at blaming others and finding fault but are unable to look within (spiritual) and change ourselves first.



DATA CAFE

Girl, interrupted

Data from a UN report shows India has one of the worst gender disparities for under-5 mortality

THE INDIAN GOVERNMENT woke up to the problem during the 1991 census. By 2001, the problem had worsened and the government had to work in mission mode to correct the skewed sex ratio. Measures like Beti Bachao, Beti Padhao have since helped, but data in a new UN report highlights that the country has one of the worst track records for gender disparities in child mortality.

Although the report UN doesn't name the countries, it says seven countries fared badly as far as under-5 mortality for girls coming in above the expected rate (based on global patterns) is concerned.

The UN Inter-agency Group for Child Mortality Estimation in *Levels & Trends in Child Mortality Report 2019* shows 6.2 million deaths of children aged 0-14 years occurred in 2018. Sub-Saharan Africa accounted for around 2.8 million under-five children deaths (52% of all global deaths), and Central and Southern Asia accounted for another 1.5 million (29%).

Around half of all under-five deaths, the report found, occurred in India, Pakistan, Nigeria, the Democratic Republic of Congo, and Ethiopia. While a higher average mortality rate for boys than for girls is the global trend, in some countries, including India, the under-5 death rate for girls is higher than for boys.

In India, the under-five mortality rate for boys, in 2018, was 36 per 1,000 population while that for girls was 37. According to the Sample Registration System 2017, the infant mortality rate (IMR) for boys and girls was 33 and 36, respectively.

The gap is worse in terms of under-five mortality rate (U-5MR) where, in 2014, the U-5MR was 51 for boys, and 59 for girls. It is crucial that the government of India pay heed to this as the continued burden on women's health—from childhood to adolescence to motherhood—far exceeds that of men.

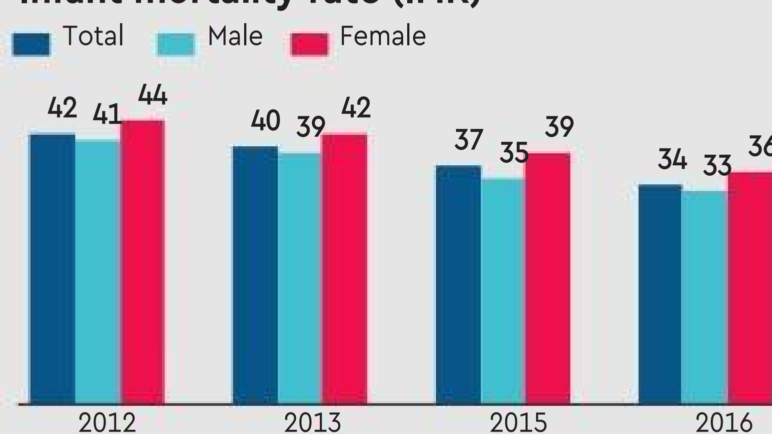
India has surely made major improvements with respect to maternal and child care, but it still has a long way to go. It needs to enhance implementation of its maternal and child healthcare policies, especially in states with higher gaps—Jharkhand (gap of 8), Assam (gap of 6), Haryana (gap of 6), Uttar Pradesh (gap of 5), Rajasthan (gap of 4), and Bihar (gap of 4).

While huge strides have been made in reducing child mortality—mortality rate for children under five years of age has declined by 59% since 1990, and mortality amongst children aged 5-14 years declined by 53%—the burden still remains high.

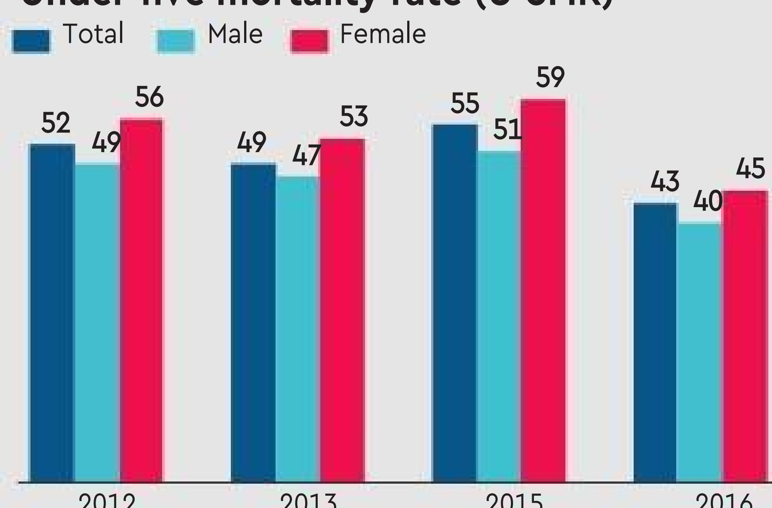
International commitments like the UN Strategy for Women's, Children's and Adolescents' Health (2016-2030) and Sustainable Development Goals (SDGs), too, were framed keeping in mind the global burden of child mortality. Until, countries like India don't work on female health, the world cannot shed this global burden.

ARJUN MUKHERJEE

Infant mortality rate (IMR)



Under-five mortality rate (U-5MR)



Source: NITI Aayog, SRS

AIF

Pass through for all

The government should consider according a tax pass through status to Category-III AIFs

DAKSHA BAXI & SURAJKUMAR SHETTY

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ALTERNATIVE INVESTMENT FUND is an investment pooling vehicle, according a significant opportunity to sophisticated investors to make medium to substantial investments. Typically, it is a pooling vehicle, permitted to be established or incorporated in India as a trust, company, limited liability partnership or a body corporate which is a privately pooled investment vehicles with Indian or foreign investors (Contributors) and registered with SEBI under the SEBI (AIFs) Regulations, 2012.

The AIF Regulations contemplate 3 categories of AIFs: (a) Category-I AIF, which generally invests in start-up or early stage ventures; (b) Category-II AIF, which is an AIF that does not fall in Category I or III such as private equity fund, debt fund, etc.; and (c) Category-III AIF, which employs diverse or complex trading strategies and may employ leverage (eg hedge fund).

The Indian tax law grants special tax pass through status to Category-I and Category-II AIFs. In effect, this means that the AIFs are ignored as entity for the purposes of taxation of income from investments. There is a legal presumption that the investor directly makes such investment, and, hence, the income received by the AIF is taxed in the hands of the investor, based on the tax provisions applicable to such investor. However, since legally the investment is made by the AIF entity and the income from the investment is actually received by the AIF, the law requires that the AIF withhold appropriate tax from the amount of income credited or distributed to the investor at the rates applicable to the investors. The investors are required to offer such income to tax in their annual tax returns and claim credit for the taxes withheld by the AIF. This pass through status is not given in respect of 'business income' of the AIF. In case of business income, the AIF itself is taxed on it and then there is no withholding when such income is distributed by the AIF to the investor.

Previously, the AIF was not permitted to pass on its losses to the investors. This lead to an anomaly where investors were being taxed on the income, but were not given benefits of losses incurred from the investments. This has now been rectified. Category I and II AIFs can now pass on their losses to investors, subject to conditions.

Despite the intention of the law being to grant a pass-through status, it is to be noted that there is an anomaly as a result of which this is not achieved. This arises from the fact that the AIF would have expenses in the form of fees to the fund manager and other administration expenses. Commercially, and legally the fund manager is permitted to deduct these from the income of the AIF and if the balance after such deduction is negative, not make distribution. However, the investor is not given the benefit of this expense (unless such an expense is related to transfer or acquisition of the relevant asset being transferred). The investor is taxed on the income received by the AIF from the investment, disregarding the fees paid to the fund manager, which is allocated to her in the proportion of her investment in the AIF. This results in the investor paying tax on income which she does not receive where the fund management expenses are more than the income. To this extent, no pass through is achieved. It is desirable that an appropriate change be made to the provisions to permit availability of fund management expenses to the investor on pass through basis so that the investor can claim deduction for them while filing returns.

As stated earlier, any income of Category I and II AIFs which is in the nature of 'business income' is taxable at the level of the AIF. Characterisation of income, from sale of investments, as 'business income' or 'capital gains' has historically resulted in tax disputes. While the tax department has issued circulars laying down principles to be applied for classification of income, there still remains a certain level of ambiguity. The government had clarified this stance in the context of FPIs, and amended the law to reflect the understanding that all investments in securities by FPIs would be considered as capital assets and therefore, income from such investments would be classified as 'capital gains'. A similar clarification is needed so that the characterisation of income from transfer of investments by AIFs is NOT treated as 'business income'.

The government may also consider according a tax pass through status to Category-III AIFs. Currently, the Indian tax laws do not contain any specific provisions governing taxability of Category III AIFs. Typically, these are structured as trusts and the laws governing taxability of trusts are used for determining taxability of Category-III AIFs and their investors. The government has, time and again, stated that its agenda is to bring certainty in tax laws and avoid litigation. Combining Category III AIFs with Category I and II AIFs, will help the Government in achieving these objectives. Investment in AIFs can be a major mobiliser both for foreign investors as well as high net worth individuals and family offices.

The recent downturn in the market and the increased risk of NPAs may to some extent be doused by increased investments by AIFs. With enough clarity and push for investments, AIFs may become a major mode of sourcing funds for investments.