

Regulatory Hotline

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STAMP DUTY STUMPS BROKERS AND DEMAT TRANSFERS

- Indian Stamp Act is proposed to be amended to replace broker turnover stamp duty with stamp duty on the clearance list used for transactions through stock exchange.
- Stamp duties to be collected by the stock exchanges or their authorised clearing corporations and the depositories on behalf of various State Governments.
- No more stamp duty waivers on transfer of securities and mutual fund units in dematerialised form.

BACKGROUND

Stamp duty considerations are important for any commercial or business transaction, especially when some States impose high stamp duties on documents to shore up their revenues, as compared to others. The Constitution of India, vide the Seventh Schedule, empowers the Union Government and the State Governments to legislate provisions regarding stamp duties as per their competence.

By virtue of the power vested in the Union Government, the Hon'ble Minister of Finance Shri Arun Jaitley had, during the budget speech of 2018-2019 announced, that reform measures with respect to stamp duty regime on financial securities transactions will be taken in consultation with the States and accordingly necessary amendments shall be made to the Indian Stamp Act, 1899 ("**Stamp Act**"). Consequently, the Finance Bill, 2019 ("**Finance Bill**"), tabled before the parliament post the budget speech of 2019-20 by the acting Hon'ble Minister of Finance Shri Piyush Goyal, introduced certain amendments to the Stamp Act that proposes to streamline the stamp duty regime on financial securities transaction in India.

In recent times, the process of financial securities transactions has evolved significantly and thus the need for the Stamp Act to keep up became imperative. Today majority of financial securities transactions are done electronically through the stock exchange or their authorised clearing corporations and the depositories. This has led to development of new and advance modes of issue or exchange of financial securities. In order to address the ambiguities and uncertainties in the stamp duty regime consequent to such technological changes, the Union Government has proposed some important reforms along with necessary clarifications. We have discussed below some of the key reforms proposed under the Finance Bill.

NEW DEFINITIONS

The Finance Bill seeks to modify definitions of some of the existing terms that have become archaic over time and bring them in line with the definitions of such terms provided under other statutes. It also seeks to introduce few new definitions that have become imperative in light of the evolution in the process of financial securities transactions. Following are some of the key definitions as proposed in the Finance Bill:

- (a) **Allotment list** means a list containing details of allotment of the securities to allottees that the issuer is required to intimate to the depository, before their names are recorded as the beneficial owner of the security as per Section 8(2) of the Depositories Act, 1996.
- (b) **Clearance list** is a list of transactions of sale and purchase relating to contracts traded on the stock exchanges. It is to be submitted to a clearing corporation in accordance with the law.
- (c) The definition of **Instrument**, is expanded to include any document, electronic or otherwise, created for a transaction in a stock exchange or depository by which any right or liability is, or purports to be, created, transferred, limited, extended, extinguished or recorded; and any other document mentioned in Schedule I of the Stamp Act. However, the definition for the purpose of Stamp Act may not include such instruments that may be specified by the Government, by notification in the Official Gazette.
- (d) **Market value**, in relation to an instrument through which—
- any security is traded in a stock exchange, means the price at which it is so traded;
 - any security which is transferred through a depository but not traded in the stock exchange, means the price or the consideration mentioned in such instrument;
 - any security is dealt otherwise than in the stock exchange or depository, means the price or consideration mentioned in such instrument.

NO MORE STAMP DUTY WAIVERS ON TRANSFER OF SECURITIES AND MUTUAL FUND UNITS IN DEMAT FORM

As per Section 8A (c) (ii) and (iii) of the Stamp Act, transfer of beneficial ownership of securities and the beneficial ownership of units, such units being units of a Mutual Fund including units of the Unit Trust of India established under Unit Trust of India Act, 1963, that are dealt by a depository, are not liable to stamp duty under the Stamp Act or any

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law for the time being in force.

The Finance Bill seeks to amend Section 8A of the Stamp Act to remove the waiver of stamp duty allowed on transfer of beneficial ownership of securities and the beneficial ownership of mutual fund units that are dealt by a depository.

Analysis: The above said waiver under the Stamp Act incentivised share transfers and investment in mutual fund units in dematerialised form due to reduced cost. However, the proposed change while at one hand will shore up revenues of the State Governments, on the other it is likely to increase the cost of commercial transactions and mutual fund investments.

STAMP DUTY ON STOCK EXCHANGE BASED TRANSACTIONS

Stamp Act imposes stamp duty to be paid on a note or memorandum sent by a broker or agent to its principal intimating the sale or purchase on account of such principal of any stock or marketable security. Similar provisions have also been iterated in various State stamp laws having either similar or varied rates of stamp duty. However, with the advent of proprietary trading in the Indian markets by the SEBI-registered brokers, where there is no exchange of note or memorandum between a broker and its principal and broker trades on its own account, there were uncertainties in the markets as to whether broker turnover stamp duty applies on proprietary trading.

To overcome these issues, various States including, among others, Maharashtra, Delhi, Gujarat, Karnataka and West Bengal amended their respective stamp laws to levy stamp duty on any record of transaction (electronic or otherwise) effected by a trading member through a stock exchange. Consequently, all proprietary trades were made subject to stamp duty in these States.

Now, under the Finance Bill, the Union Government in consultation with the State Governments has decided to remove the requirement of broker turnover stamp duty which was payable to the State Government on any note or memorandum or any other document, electronic or otherwise, associated with transactions done through the stock exchange, and replace it with stamp duty payable on each sale or purchase of securities, whether delivery based or otherwise, through a stock exchange and consequently listed in the clearance list. The stamp duty on each such sale or purchase in the clearance list shall be collected on behalf of the State Government by the stock exchange or a clearing corporation authorised by it, from its buyer, on the market value of such securities at the time of its settlement, as per the rates specified in Schedule I of the Stamp Act (refer to the table below). Further, the clearance list shall be regarded as the principal instrument for the purpose of payment of stamp duty and no stamp duty shall be levied upon any other instrument (subject to stamp duty otherwise) involved in the above said sale or purchase.

| Instruments | Rate of Stamp Duty |
|--|--------------------|
| DEBENTURE | |
| a) issue | 0.005% |
| b) transfer or re-issue | 0.0001% |
| SECURITY OTHER THAN DEBENTURES | |
| a) issue | 0.005% |
| b) transfer on delivery basis | 0.015% |
| c) transfer on non-delivery basis | 0.003% |
| d) derivatives- | |
| (i) futures (equity and commodity) | 0.002% |
| (ii) options (equity and commodity) | 0.003% |
| (iii) currency and interest rate derivatives | 0.0001% |
| (iv) other derivatives | 0.002% |
| e) Government securities | 0% |
| f) repo on corporate bonds | 0.00001% |

Analysis: Upon notification of above said amendments, the stamp duty shall be applicable on the sale or purchase listed in the clearance list and not upon exchange of a note or memorandum as it currently is. Further, the onus of stamp duty payment is on the buyer in such transaction. Thus, it is likely that the position of proprietary trades may now be clear and such activities going forward may fall within the scope of stamp duty payable on stock exchange based transactions.

STAMP DUTY ON DEPOSITORY BASED TRANSACTIONS

Section 8A of the Stamp Act requires an issuer of securities, through one or more depositories, to pay stamp duty in respect of such securities on the total amount of the security issued by it and such securities need not be stamped. This requirement under the Stamp Act has been the basis for levying stamp duty on shares/securities issued by a company in the dematerialised form.

In relation to issue of securities, the Finance Bill states that if such issue of securities leads to any creation or change in the records of a depository, the stamp duty on the list containing details of allotment of the securities (i.e. allotment list) shall be collected on behalf of the State Government by the depository, from the issuer of securities on the total market value of the securities contained in such list.

The Finance Bill further lays down the provisions for levy of stamp duty in case where the transfer of securities for a consideration, whether delivery based or otherwise, is made by a depository and such transaction is not a stock exchange based transactions. In this regard, the Finance Bill states that the stamp duty on such transfers shall be collected on behalf of the State Government by the depository from the transferor of such securities on the consideration amount specified therein.

Analysis: Issue of shares in dematerialised form has been subject to payment of stamp duty since the introduction of

Section 8A of the Stamp Act, despite such issue not being accompanied by an instrument, such as a share certificate in case of physical issue of shares. However, to further streamline the process, the Finance Bill introduces the concept of allotment list in the Stamp Act and further delegates the responsibility for collection of related stamp duties on the depository through which such issue of securities shall be done.

Further, in relation to the stamp duty imposed on transfer of dematerialised securities upon removal of the exemption discussed in the section above, the Finance Bill also lays down the mode of levying stamp duties on such transfer through the depositories.

STAMP DUTY ONLY ON PRINCIPAL INSTRUMENTS

As per Section 4 of the Stamp Act, in the case of any sale, mortgage or settlement, where several instruments are employed for completing the transaction, it is only the principal instrument that shall be chargeable with stamp duty as per the prescribed rates and each of the other instruments shall be chargeable with a duty of one rupee instead of the duty (if any) specifically prescribed for such other instrument.

The Finance Bill has now proposed that in case of stock exchange or depository based transactions discussed in the sections above, it is only the instrument on which stamp duty is chargeable under the respective heads that shall be regarded as the principal instrument for the purpose of levying stamp duty and no stamp-duty shall be charged on any other instruments relating to any such transaction.

ONUS OF STAMP DUTY PAYMENTS

In light of the above mentioned changes introduced by the Finance Bill, the next obvious question is that who shall bear the brunt of newly introduced stamp duties. To address this, the Finance Bill further seeks to amend Section 29 of the Stamp Act that sets out responsibility of relevant party to a transaction for payment of stamp duty applicable under the Stamp Act.

| Nature of Transaction | Birder of Stamp Duty Payment |
|--|---|
| Sale of security through stock exchange | Buyer |
| Sale of security otherwise than through a stock exchange | Seller |
| Transfer of security through a depository | Transferor |
| Transfer of security otherwise than through stock exchange or depository | Transferor |
| Issue of security, whether through a stock exchange or a depository or otherwise | Issuer |
| In case of any other instrument not specified in Section 29 of the Stamp Act | Person making, drawing or executing such instrument |

PENALTIES

A new Section 62A has been proposed to be inserted in the Stamp Act to prescribe penalties for default by the stock exchange or a clearing corporation or the depository in collecting the stamp duties or transferring the same to the respective State Governments within 15 days of the expiry of the specified time. Failure to collect or transfer the stamp duty within the specified time will attract a penalty of not less than one lakh rupees, and which may extend up to one per cent of the collection or transfer amount so defaulted. Further, any failure to submit information, or submission of false document or declaration by the above mentioned entities, shall be penalized with a fine of one lakh rupees (approx. USD 1400) for each day during which such failure continues or one crore rupees (approx. USD 143,000), whichever is less.

Analysis: Section 62A has been introduced in furtherance of Section 9A. Section 9A prescribes the (i) method and (ii) amount of stamp duty to be collected by the stock exchanges, clearing corporations or depositories, for transactions undertaken on stock exchanges or depositories. Penalizing such non-compliance by these entities will thus help in stopping of leakages. Since stock exchanges, clearing corporations or depositories already have the details of the person undertaking such transactions, it will be easier to directly credit the stamp duty to the concerned State, although it will be an additional administrative burden. Further, provisioning of a timeline will also ensure that timely transfer of funds takes place. Additionally, this will discourage non-submission of details or submission of fake documents. The section therefore, warrants that the Government receives funds, information and documents all on time.

CONCLUSION

After several unsuccessful attempts to amend the Stamp Act over the past several years, the Union Government has finally managed to convince the States to streamline the stamp duty regime for financial securities transaction and accordingly the above discussed reforms have been introduced by the Finance Bill. These amendments once notified, will remove the uncertainties pertaining to applicability of stamp duties on proprietary trades or transfer of shares of a company in dematerialised form.

Further, it is important to note that while the Union Government, pursuant to the Finance Bill, has bestowed the responsibility of collection of stamp duties in specified cases on the stock exchanges or their authorised clearing corporation or the depository on behalf of the State Government, the detailed process for the same would also have to be separately notified by the Government by introducing necessary rules in this regard.

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