Stamp Duty stumps brokers and demat transfers

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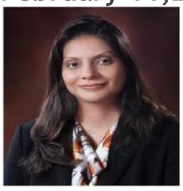

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Background

Stamp duty considerations are important for any commercial or business transaction, especially when some States impose higher stamp duties on documents to shore up their revenues, as compared to others. By virtue of the power vested in the Union Government, the Minister of Finance, Government of India 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 and accordingly necessary amendments shall be made to the Indian Stamp Act, 1899 ("**Stamp Act**"). Consequently, the Finance Bill, 2019 ("**Finance Bill**"),[1] introduced certain amendments to the Stamp Act that proposes to streamline the stamp duty regime on financial securities transactions in India.

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 advanced modes of issue or exchange of financial securities, and thus the need for the Stamp Act to keep up became imperative. In order to address the ambiguities and uncertainties consequent to such technological changes, some important reforms have been proposed under the Finance Bill, which we have discussed below.

New Definitions

The Finance Bill seeks to modify definitions of some existing terms that have become archaic over time, and 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.[2]

(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 includeany 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, it may not include such instruments that may be specified by the Government.

(d) **Market value**, in relation to an instrument through which —

(i) any security is traded in a stock exchange, means the price at which it is so traded;

(ii) 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;

(iii) 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 mutual fund units[3], that are dealt by a depository, are not liable to stamp duty. The Finance Bill seeks to amend Section 8A of the Stamp Act to remove the waiver of stamp duty allowed on such transfer of beneficial ownership.

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. However, with the advent of proprietary trading by SEBI-registered brokers, there were uncertainties in the markets as to whether broker turnover stamp duty applies on proprietary trading, since there is no exchange of note or memorandum.

To overcome these issues, various States[4] 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 such States.

Now, the Finance Bill 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 replaced 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 shall be collected on behalf of the State Government by the stock exchange or a clearing corporation, 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).

Instruments	Rate of Stamp Duty
DEBENTURE	
a) issue	0.0005%
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 going forward proprietary trades 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 regarding such securities on the total amount of the security issued by it and such securities need not be stamped. Thereby, requiring the levying of stamp duty on shares/securities issued in the dematerialised form.

The Finance Bill states that forthwith, if such issue of securities leads to any creation or change in the records of a depository, the stamp duty on the 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.

Furthermore, in cases where transfer of securities for a consideration (delivery based or otherwise) is made by a depository and such transaction is not a stock exchange based transaction, stamp duty 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. However, to further streamline the process, the concept of allotment list has been introduced which further delegates the responsibility for collection of related stamp duties on the depository through which such issue of securities shall be done.

Further, regarding 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 and each of the other instruments shall attract a duty of one rupee instead of the prescribed duty (if any).

The Finance Bill has now proposed that in case of stock exchange or depository based transactions, only the instrument on which stamp duty is chargeable under the respective heads discussed above, shall be regarded as the principal instrument 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. The Finance Bill addresses this by amending Section 29 of the Stamp Act. It sets out responsibility of relevant party to a transaction for payment of applicable stamp duty as follows: 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;[5] and failure to submit information, or submission of false document or declaration by the above mentioned entities,[6] will attract the prescribed penalties.

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 specified entities, for transactions undertaken on stock exchanges or depositories. Penalizing such non-compliance by these entities will thus help in stopping of leakages. They can now directly credit the stamp duty to the concerned State, although it will be an additional administrative burden. 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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[1] The Finance Bill was tabled before the parliament post the budget speech of 2019-2020 by the acting Hon'ble Minister of Finance Shri Piyush Goyal.

[2] Intimation to the depository shall take place before the names of the allottees are recorded as the beneficial owner of the security as per Section 8(2) of the Depositories Act, 1996

[3] Such units being units of a Mutual Fund including units of the Unit Trust of India established under Unit Trust of India Act, 1963.

[4] Including, among others, Maharashtra, Delhi, Gujarat, Karnataka and West Bengal.

[5] 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.

[6] 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.