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Tax News

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Union Budget 2011

India

Discussion on budget highlights

G. Joseph & Associates

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Letter to the reader

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Dear Reader,

We are pleased to present you a discussion on the Union Budget for the financial year 2011 – 2012 (the Finance Bill, 2011) presented by the Honorable Finance Minister, Mr. Pranab Mukherjee at the Lok Sabha on 28 February 2011

As compared to the rest of the world, India came out of the global financial crisis with relative ease. While the lower than expected industrial growth rate and high inflation continue to be a cause for concern, most investors, industry leaders and the work force continue to have faith in the Indian growth story

Through this issue of 'Tax News' as part of GJA Learning series, we hope to provide you a snap-shot of some of the key takeaways from the budget speech. While further clarity to many of the amendments will unravel during the coming days, we believe that you will benefit from the early insights from the Budget which may affect your business and personal wealth

Should you require any further clarifications or details on the budget proposals or any assistance in the analysis of the impact of the proposals on your business, please do feel free to get in touch with us. Further, we always look forward to your valuable suggestions.

Yours faithfully

George Joseph
Managing Partner

Contents

Executive summary

Macro economic outlook	► GDP is expected to grow at 8.6% during 2010-11 and 9.0% during 2011-12 as against the growth rate of 8.0% during 2009 -10 ► Fiscal deficit is anticipated to close at 5.1% in 2010-11 and expected to reduce to 4.6% during 2011-12.
Direct taxation Key areas of amendments include : ▪ Revision of taxation slabs for individual assessees ▪ Surcharge applicable for domestic corporate assessees has been reduced by 2.5% ▪ MAT rate has been increased by 0.5% ▪ The anticipated extension of the STPI tax holiday scheme did not find a place in the Finance Bill, 2011	► Individual assessees have received benefits in the form of increase in the basic exemption limits and through the creation a new category of 'very senior citizens'. ► The Central Government is expected to exempt salaried tax payers from filing their returns of income ► Surcharge applicable for domestic corporate assessees has been revised to 5.0% from the present 7.5% ► MAT rate has been increased to 18.5% from the present 18.0% ► Alternate Minimum Tax has been introduced for LLPs at 18.5% of adjusted book profits. ► Exemption from MAT for SEZ units have been withdrawn. SEZ units will now be required to remit MAT of 18.5% of book profits. ► Exemption from Dividend Distribution Tax for SEZ developers and operators have been withdrawn. ► The income tax holiday for STPI units which expires on March 31, 2011 was not extended.
Indirect taxation Key areas of amendments include : ▪ General excise duty, customs duty and service tax rates have been left unchanged at 10.0% ▪ Customs procedure for import and export have been simplified ▪ Service tax net has been widened to add new services.	► The peak rates of excise and basic customs duty and effective rate of service tax have been left unchanged at 10.0%. ► Nominal excise duty of 1.0% has been introduced for 130 items. ► Customs procedure for clearance of imports and exports will now be on self assessment basis. ► Interest on delayed payment has been increased to 18.0% from 13.0% ► Service tax extended to services by air conditioned restaurants having liquor licenses and to short term accommodation in hotels. ► The implementation of the Goods & Service Tax has been rescheduled to 1 April 2012.

Direct taxation

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Key highlights

- The Budget 2011 has reduced the age of senior citizens from 65 years to 60 years. It has also created a new classification of 'Very Senior Citizens' who are 80 years or more.
- Tax slabs for women remained unchanged

Direct taxation

- The key changes in the Direct taxation contemplated by the Finance Bill, 2011 are presented below

Change in taxation slabs

- The Finance Bill, 2011 has revised the income tax slabs for individual assesses, as illustrated below:

A) In case of women other than senior citizens (No change)

2010-11 slab	Tax rate	2011-12 slab	Tax rate
Below INR 1.9 lakhs	NIL	Below INR 1.9 lakhs	NIL
INR 1.9 lakhs to INR 5.00 lakhs	10.0%	INR 1.9 lakhs to INR 5.00 lakhs	10.0%
INR 5.0 lakhs to INR 8.00lakhs	20.0%	INR 5.0 lakhs to INR 8.00lakhs	20.0%
Above INR 8.0 lakhs	30.0%	Above INR 8.0 lakhs	30.0%

B) In case of senior citizens

Individuals who are 65 years or more		Individuals who are 60 year or more, but less than 80 years	
2010-11 slab	Tax rate	2011-12 slab	Tax rate
Below INR 2.4 lakhs	NIL	Below INR 2.5 lakhs	NIL
INR 2.4 lakhs to INR 5.00 lakhs	10.0%	INR 2.5 lakhs to INR 5.00 lakhs	10.0%
INR 5.0 lakhs to INR 8.0 lakhs	20.0%	INR 5.0 lakhs to INR 8.0 lakhs	20.0%
Above INR 8.0 lakhs	30.0%	Above INR 8.0 lakhs	30.0%

C) In case of very senior citizens

2009-10 slab	Tax rate	2011-12 slab	Tax rate
NA	NA	Below INR 5.00 lakhs	NIL
NA	NA	INR 5.0 lakhs to INR 8.0 lakhs	20.0%
NA	NA	Above INR 8.0 lakhs	30.0%

Key highlights

- In the case of male non – senior citizens, the Budget 2011 has raised the basic exemption limit from INR 1.6 lakhs to INR 1.8 lakhs which will translate into a tax saving of around INR 2.0 thousand

D) In case of other individuals

2010-11 slab	Tax rate	2011-12 slab	Tax rate
Below INR 1.6 lakhs	NIL	Below INR 1.8 lakhs	NIL
INR 1.6 lakhs to INR 5.0 lakhs	10.0%	INR 1.8 lakhs to INR 5.00 lakhs	10.0%
INR 5.0 lakhs to INR 8.0 lakhs	20.0%	INR 5.0 lakhs to INR 8.00 lakhs	20.0%
Above INR 8.0 lakhs	30.0%	Above INR 8.0 lakhs	30.0%

Key highlights

- Surcharge for domestic corporates has been reduced to 5.0% from 7.5% and for foreign corporates from 2.5% to 2.0%
- MAT has been made applicable to SEZ units and developers.
- Dividends from foreign subsidiaries of Indian corporates will be taxed at a lower rate of 15.0% in order to encourage them to return funds to India.
- A major advantage of the LLP structure over a company structure has disappeared through the introduction of AMT of 18.5% of adjusted book profits

Reduction of surcharge for corporate assessees

- Surcharge has been reduced from 7.5% to 5.0% for corporate assessees having taxable income exceeding INR 100.0 lakhs.
- Surcharge for non domestic corporate assessees having taxable income exceeding INR 100.0 lakhs has been marginally reduced from 2.5% to 2.0%

Taxation of foreign dividends at a reduced rate

- Dividend received by Indian companies from their foreign subsidiaries will be taxed only at 15.0% plus applicable surcharge and cess as against the current rate of 30.0%

MAT made applicable to SEZ units and developers

- SEZ units and developers will now be subject to MAT. Corporate assessees having units in SEZs or developing SEZs will now be required to pay MAT at the rate of 18.5% of their book profits.

Applicability of Dividend Distribution Tax ('DDT') to SEZ developers and operators

- SEZ developers and operators were exempted from payment of DDT of 16.61% of dividend declared. This benefit has been withdrawn for dividend declared, distributed or paid after June 1, 2011.

Increase in MAT rate

- Rate of MAT has been increased from 18.0% to 18.5% of book profits of corporates.

Introduction of Alternate Minimum Tax ('AMT') for Limited Liability Partnerships ('LLP')

- The Finance Bill, 2011 proposes to introduce an AMT which will be imposed on LLPs at the rate of 18.5% of the adjusted total income. AMT will be eligible for tax credit similar to that of MAT credit which will be the excess of AMT paid over and above the regular income tax due. LLPs can carry forward this credit of AMT for the next ten years.

Amendment in the definition of 'Charitable Purposes' under Section 2(15)

- The Finance Act, 2010 had amended the definition of 'charitable purposes' to include " the advancement of any other object of general public utility" which involves the carrying on of trade, commerce, or business subject to the condition that the receipts from such activities shall not exceed INR 10.0 lakhs. The Finance Bill, 2011 proposes to increase this monetary limit from INR 10.0 lakhs to INR 25.0 lakhs.

Infrastructure debt funds

- The Central Government is now empowered to notify infrastructure debt funds whose income will be exempt from tax.
- Non residents who invest and receive interest from such funds will be taxed only at 5.0% of the gross amount of the interest received.

Key highlights

- The benefits of investment in infrastructure bonds under Sec. 80CCF has been extended for one more year
- Assessees who are required to furnish transfer pricing certificates have time until November 30th to file their return of income

Increase in weighted deduction for contributions made for approved scientific research programme

- Presently, a weighted deduction of 175.0% is allowed on all contributions to a National Laboratory or a university or and Indian Institute of Technology or a specified person for the purpose of an approved scientific research programme. This weighted deduction of 175.0% is now being increased to 200.0%.

Investment linked deductions for housing and fertilizer projects

- Investment in affordable housing projects and fertilizer projects will be eligible for a deduction of expenditure of capital nature (other than land, goodwill, and financial instruments) under Section 35AD.

Rationalisation of taxation of the New Pension System (NPS)

- Contribution by the employer and the employee to the NPS is eligible for a deduction under Sec. 80CCD. The aggregate deduction claimed under various sections, viz., 80C, 80CCC and 80CCD could not exceed INR 1.0 lakh. It has now been proposed to exclude the employer's contribution to the NPS from the eligible deduction.
- Employers will now be permitted to claim their contribution to the NPS as a deduction to the extent that the contribution does not exceed 10.0% of the employees' salaries.

Deduction for investment in long term infrastructure bonds

- Sec. 80CCF was introduced by the Finance Act, 2010 which gave a deduction of INR 20.0 thousand for investment in long term infrastructure bonds over and above the normal deduction of INR 1.0 lakhs. It was originally planned to have this deduction only for the financial year 2010 – 11. This deduction is now being extended to the financial year 2011 – 12.

Determination of Arm's Length Price ('ALP') in transfer pricing

- For the purpose of transfer pricing, the ALP for a transaction is required to be determined. If the variation between the actual price of the transaction and the ALP determined does not exceed 5.0%, then no adjustments will be made and the actual price will be taken as the ALP. The Finance Bill, 2011 proposes to withdraw the blanket margin of 5.0% across all segments and notify different percentages.

Additional powers to Transfer Pricing Officers ('TPO')

- Presently, the jurisdiction of the TPOs is limited to the determination of the ALP of transactions which are referred by the Assessing Officers. The Finance Bill, 2011 proposes to empower TPOs to extend the determination of ALP to other transactions which are noticed by him.

Key highlights

- The Central Government is expected to exempt salaried tax payers from filing their return of income.

`of due date of filing of return of income in transfer pricing cases

- Assessees who have entered into international transactions with associated enterprises and who are required to file a transfer pricing report from a chartered accountant in Form 3CEB have additional time till November 30th to file their return of income as against September 30th/July 31st for other assessees.

Exemption for filing of return of income

- The Central Government has been empowered to notify class or classes of persons who are not required to file their returns of income. In all likelihood, this will include salaried employees whose income comprises of only salary and in whose case employers discharge their entire tax liability through TDS.

Reporting of activities of liaison offices

- Liaison offices of foreign entities were not required to file their return of income in India as no business activities were permitted to be carried out in India. The Finance Bill, 2011 proposes to require liaison offices to report on their activities within 60 days from the end of the financial year.

Indirect taxation

Excise duty

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Key highlights

- The general rate of excise duty has been left unchanged at 10.0%
- Nominal excise duty of 1.0% has been introduced on 130 items.
- Interest on delayed remittance of duty will now entail interest of 18.0% as against the present 13.0%

Peak rate of duty maintained , but concessional rate of duty increased

- The peak rate of duty has been maintained at 10.0%. Concessional rate of duty of 4.0% has been increased to 5.0%. As a result, items such as prepared food stuffs, paper and paper articles, textile intermediates and textile goods, drugs, medical equipment, etc. would now be subject to the enhanced rate of duty of 5.0%.

Additional Excise Duty ('AED') removed

- AED imposed under the AED (GSI) has been removed on sugar, textiles and textile products. This is in order to enable states to levy VAT.

Nominal duty introduced

- Nominal duty of 1.0% without availment of Cenvat input credit has been imposed 130 items which were earlier exempted.

The impact of Budget 2010 on key sectors are as follows:

Cement

- Rate of excise duty on cement and cement clinker have been revised. Cement cleared in packaged form with a retail sale price exceeding INR 190 per 50 Kg bag will now be subject to excise duty of ad valorem rate 10**% + INR 160.0 per tonne.**

Readymade garments and textile articles

- Readymade garments and textile articles which are sold under a brand name will now be subject to excise duty of 10.0%

Automobile sector

- The Taxi Refund Scheme is being extended to include vehicles carrying 13 persons including the driver.

Food /agro processing, and agriculture industries

- Full exemption from excise duty is being extended to air-conditioning equipment, panels and for installation of cold chain infrastructure for the preservation, storage, transport or processing of agricultural, horticultural, dairy, poultry, apiaries, aquatic and marine produce.

Amendments in Central Excise Rules and Cenvat Credit Rules

- Interest for delayed remittance of duty has been increased from 13.0% to 18.0%
- Rule 6(5) of the Cenvat Credit Rules which specified certain input services which were eligible for full Cenvat credit unless they were used exclusively for exempted operations has been deleted.
- The definition of exempted services has been amended to specifically include trading activities. This will impact the computation of credit reversal in cases where a person carries on trading activities along with manufacture of excisable products or provision of taxable services.
- It has been specifically provided that service tax paid under Reverse Charge Mechanism on import of services will be eligible for Cenvat input credit. This amendment is with retrospective effect.
- Definition of inputs and input services has been substituted to exclude goods and services used for the following:
  - Construction of building or civil structure, laying of foundation for support of capital goods.
  - Outdoor catering or use in guest house, residential colony, club or recreation facility when such goods or services are primarily used for personal use or consumption of employees.
  - Services such as beauty treatment, health services, health and fitness centre, life insurance which are primarily used for personal use or consumption of employees.

Key highlights

- The general rate of excise duty has been left unchanged at 10.0%
- Nominal excise duty of 1.0% has been introduced on 130 items.
- Interest on delayed remittance of duty will now entail interest of 18.0% as against the present 13.0%

Penal provisions have been amended

- In cases where transactions to which duty is liable has been appropriately shown in the assessees records, penalty will be reduced to 50.0% of the duty.
- In cases where duty along with interest is paid before the issuance of a show cause notice, penalty can be compounded to 1% per month subject to a maximum of 25% of duty. The aforementioned reduced penalty provisions will not be applicable in cases of fraud, suppression, misstatement or collusion.
- Recovery of Central excise dues has been strengthened by creating a first charge on the property of the defaulter.
- The Joint Commissioner or the Additional Commissioner of Central Excise are now empowered to himself or to authorise any other central excise officer to conduct a search of an assessee’s premises.

Indirect taxation

Customs duty

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Key highlights

- No changes have been proposed on the general rates for customs duty.
- Customs procedure for imports and exports have been simplified to a great extent by introducing payment on self assessment basis

Peak rate of duty maintained

- The peak rate of basic customs duty has been left unchanged at 10.0%.
- The sector wise implications of the Budget proposals are as follows:

Special Economic Zone ('SEZ')

- All clearances from SEZ to the Domestic Tariff Area ('DTA') will now be eligible for exemption from SAD provided they are not exempted from the levy of VAT / sales tax.

Ship Repairs

- The benefit of exemption available to ship repair units on import of spares and consumables required for repair of ocean going vessels is being extended to owners of such vessels registered in India.

Textiles

- Basic customs duty is being reduced on raw silk of all grades from 30% to 5%.
- Cotton waste is being fully exempted from basic customs duty.

Agriculture / Food Processing

- Basic customs duty is being reduced to 2.5% on specified agricultural machinery such as paddy transplanters, cotton picker, reaper-cum-binder, sugarcane harvesters, etc.
- De-oiled rice bran oil cake has been fully exempted from basic customs duty and an export duty of 10.0% has been imposed on its exports.

Environment-friendly items

- Concessional CVD of 5.0% (by way of central excise exemption) and full exemption from SAD is being provided to LEDs used for manufacture of LED lights.
- Basic customs duty is being reduced from 10.0% to 5.0% on solar lanterns.

Electronics Hardware

- A concessional import duty structure of 5.0% CVD and Nil SAD is being prescribed on parts of inkjet and laser printers imported for manufacture of such printers.
- Full exemption from 4% special additional duty of customs on parts, components and accessories for manufacture of mobile handsets including cellular phones, parts thereof (except accessories) has been extended upto 31 March 2012
- Full exemption from customs duty is being extended to additional specified capital goods and raw materials for the manufacture of electronic hardware.

Export Promotion

- The list of specified goods, allowed to be imported duty free for use in the manufacture of leather goods, for export is being expanded.

Amendment in Customs Act

- Existing procedure provides for assessment of every bill of entry or shipping bill by the customs officer before removal from port of import. Goods will now be allowed to be cleared both for import or export on 'self assessment' basis.
- Time limit for demanding customs duty and claiming refund of duty enhanced from six months to one year for all categories of importers.
- Interest on delayed remittance of customs duty enhanced to 18.0%
- Provisions introduced to create first charge on the property of the defaulter for recovery of the customs dues from such defaulter subject to certain conditions.

Indirect taxation

Service tax

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Key highlights

- Service tax net has been widened to include services of restaurants and hotels. Further, amendments to the definition of existing taxable services enhances the tax base

Service tax rate unchanged

- The effective service tax rate has been left unchanged at 10.3%

Service tax net widened

- The Service tax net has been widened to include the following services:
    - Services provided by air conditioned restaurants having a license to serve alcoholic beverages in relation to serving of food and / or beverages (70% abatement will be allowed)
    - Short term accommodation provided by a hotel, in, guesthouse, club or campsite or any other similar establishment for a continuous period of less than three months (50% abatement will be allowed)
- The effective date of these changes will be notified after the enactment of the Finance Bill, 2010
- Further, following amendments have been made to the existing taxable services:

Category of service	Change
Life insurance services	Scope has been expanded to cover all services provided to a policyholder or any person by an insurer carrying on life insurance business.
Club or association service	Scope has been expanded to include services provided to non members.
Authorised service station service	All motor vehicles other than those meant for goods carriage and three wheeled scooter auto-rickshaws have been covered.
Business support service	Services provided by way of operational or administrative assistance in any manner would be covered under these services.
Legal consultancy service	Services provided by a business entity to individuals in relation to advice, consultancy or assistance in any branch of law and representational services by any person to a business entity and arbitration services provided by a tribunal to a business entity have been included in the ambit of these services.
Commercial training or coaching service	All unrecognised courses have been included.
Health services	▪ All services provided by a centrally air conditioned (wholly or partially) clinical establishment having more than 25 beds ▪ Diagnostic services being provided by a clinical establishment with the aid of a laboratory or other medical equipment ▪ Services provided by a doctor not being an employee of a clinical establishment from the premises of such an establishment.

Key highlights

- Service tax net has been widened to include services of restaurants and hotels. Further, amendments to the definition of existing taxable services enhances the tax base

- The effective date of above changes will be notified after the enactment of the Finance Bill, 2010.

New exemptions

- Exemption is being provided to services provided by an organiser of business exhibitions in relation to business exhibitions held outside India.
- An abatement of 25.0% from the taxable value is being provided for the purpose of levy of service tax under 'Transport of goods through coastal and inland shipping'
- Exemption is being provided to services provided within a port or an airport under 'Works contract' service for specified purposes.
- Services related to transportation of goods by road, rail or air when both the origin and the destination are located outside India is being exempted from service tax.
- A modified scheme is being introduced to refund service tax to SEZ developers and units:

Withdrawals / amendments of Service tax

- Rates of service tax on travel by air have been increased.

Point of Taxation Rules, 2011 introduced

- The Point of Taxation Rules, 2011 will be in effect from April 1, 2011.
- Presently, the point of taxation is at the point of receipt of taxable value from the recipient of the service. With effect from April 1, 2011, the point of taxation will be deemed to be:
    - date on which service is provided or to be provided; or
    - date of invoice; or
    - date of payment;

    whichever is earlier

Others

- The Export of Services Rules, 2005 and Taxation of Services (Provided from Outside India and Received in India) Rules, 2006 are being amended so as to move some of the specified services from one category to another.
- Works Contract (Composition Scheme for Payment of Service Tax) Rules, 2007 are being amended so as to provide that input credit of tax paid under 'Erection, commissioning or installation', 'commercial or industrial construction' and 'construction of complex' services will be restricted to 40% of the tax paid.
- Penalty for delayed payment has been reduced to 1% from 2% per month . Further, the maximum penalty has been reduced to 50% of the tax amount.
- Interest for delayed payment of service tax will be increased to 18% a year (and to 15% a year for tax payers with turnover below INR 60 lakhs).
- Maximum penalty for delayed filing of return will be increased to INR 20,000.
- Benefit of reduced penalty will not be available in cases of fraud, misstatement, suppression or collusion.

Notice to the reader

Glossary

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We have used following sources while preparing this document

1. The Economic Survey of India, 2011
2. The Finance Bill, 2011
3. The Finance Minister's Budget speech , 2011

Glossary of terms:

Lakhs	: Hundred thousands
INR	: Indian Rupee
GDP	: Gross Domestic Product
STPI	: Software Technology Parks of India
MAT	: Minimum Alternate Tax
LLP	: Limited Liability Partnership
SEZ	: Special Economic Zone
CVD	: Countervailing Duty
BCD	: Basic Customs Duty
AMT	: Alternate Minimum Tax
DDT	: Dividend Distribution Tax
TDS	:Tax Deducted at Source
AED	: Additional Excise Duty
AED (GSI)	: Additional Excise Duty (Goods of Special Importance) Act
VAT	: Value Added Tax
DTA	: Domestic Tariff Area
SAD	: Special Additional Duty

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