



INDIA

INDIA BUDGET 2008

The Budget 2008, presented on 29 February 2008, came in the backdrop of robust economic growth of 8.7% in GDP in 2007-08 with the manufacturing and services sector continuing to be the twin engines of growth. The agriculture sector continues to languish with a sluggish growth rate of 2.6%. The tax collections for the year exceeded the budget estimates.

With the elections looming in the horizon, this Budget, as expected, turned out to be an election budget with a slew of measures favoring the common man especially the farmers. Of all the measures, the most significant has been the loan waiver scheme for farmers estimated to cost over INR600 billion. Though a political necessity, this is an unfortunate disincentive for credit compliance and forms a bad precedence. Also the Budget has higher allocations on the flagship programs of the United Progressive Alliance coalition Government on rural employment and urban renewal. A lot of emphasis has also been laid on education and skill development which is the need of the hour in India.

DIRECT TAXES

The proposals in the Finance Bill 2008 have major elements relating to lowering the burden on individual tax, streamlining tax administration processes, enhancing research and development, lowering cascading effect of Dividend Distribution Tax (DDT) and encouraging growth of corporate debt market.

Personal Taxation

Basic tax rates

The basic exemption limit for individuals is proposed to be revised. The new slabs are as follows:

Income (INR)	Tax Rate
Up to 150,000*	Nil
150,001 - 300,000	10%
300,001 - 500,000	20%
Above 500,000	30%

*Basic exemption for women and senior citizens will be INR180,000 and INR225,000, respectively.

There is no change proposed in respect of surcharge which will be levied at 10% on income above INR1,000,000. Education cess of 2% and additional cess called Secondary and higher education cess of 1% will continue to be levied.

Deposit made under Senior Citizen Savings Scheme Rules, 2004 and Five Year Time Deposit under the Post Office Time Deposit Rules, 1981 are proposed to be covered within the INR100,000 limit prescribed under Section 80C of the Income-tax Act, 1961 (the Act).

It is proposed to allow an additional deduction of up to INR15,000 (INR20,000 if parent's age is greater than 65 years old) to an individual on any payment made to effect insurance on the health of his parents.

Reverse mortgage scheme

It is proposed that any amount received by a senior citizen under a notified scheme of reverse mortgage will be exempt from tax. Also the pledge of the residential property under the scheme of reverse mortgage will not be regarded as a transfer of a capital asset and therefore shall not attract capital gain tax.

Corporate Taxation

Minimum alternate tax

In order to remove the ambiguity on adjustments relating to tax entries in the profit and loss account, it is proposed that the "book profits" be increased by an amount of DDT paid, amount of deferred tax paid and deferred tax provision debited to Profit & Loss Account. The amendment is proposed to be effective retrospectively from 1 April 2001.

Dividend distribution tax

In order to mitigate the cascading effect of DDT, it is proposed that any dividend received by a domestic company (C1) during any financial year from its subsidiary (C2) shall be allowed to be deducted from dividend to be declared/distributed/paid by C1, for the purpose of computing its DDT, provided that the dividends so received by C1 had been subject to payment of DDT by C2. It is also provided that that C1 should not be a “subsidiary” of any other company. For this purpose, a company shall be a subsidiary of a domestic company, if such domestic company holds more than half in the nominal value of the equity share capital of such company. The benefit under the proposal will be available to single tier companies only.

Tax holiday

The Finance Bill 2008 has proposed to provide a five-year tax holiday in respect of profits derived from the business of operating and maintaining hospital located in non metro cities which start functioning between 1 April 2008 and 31 March 2013, subject to certain conditions.

It is proposed to provide a five-year tax holiday in respect of profits derived from the business of new two, three or four star hotels located in specified district having a World Heritage Site. Such hotels should start functioning between 1 April 2008 and 31 March 2013.

It is also proposed that no tax holiday will be available to undertakings commencing business of refining mineral oil on or after 1 April 2009.

Business income

It is proposed to allow a weighted deduction of 125% in respect of any sum paid for scientific research to a domestic company engaged in scientific research and development, subject to fulfillment of certain conditions. Further, to avoid multiple deductions, it is proposed that such domestic company incurring the expenses (recipient company) would not be entitled to the weighted deduction of 150% as prescribed under the provisions of the Act.

It is also proposed that Securities Transaction Tax paid in respect of taxable securities transactions shall be deductible if the income arising thereon is considered as business income.

With a view to provide a level playing field, amortisation of post commencement preliminary expenses available to the industrial sector is proposed to be extended to all sectors including services sector.

Capital gains

Rate of short-term capital gains is proposed to be increased from 10% to 15% in relation to transfer of shares or units, which is subject to securities transaction tax.

Also it is proposed to exempt conversion of specified bonds of a company issued under foreign currency exchangeable bonds into shares or debentures of any company from capital gains tax.

Tax withholding

The scope of “assessee in default” has been proposed to be widened to include all persons who have failed to deduct tax at source.

Currently, payment can be made to non residents after submitting an undertaking and a certificate with the banker. Such documents are thereafter forwarded by the banker to the assessing officer. It is proposed to introduce a new provision under which such remittance will need to be reported to the tax authorities through e-filing system.

It has been proposed that interest payment in respect of corporate debt security listed on a recognised stock exchange in India and held in dematerialised form will not be subject to withholding tax.

The scope of withholding tax provisions in respect of payments to contractors is proposed to be widened to require association of person or a body of individuals to withhold tax on contractual payments.

The rate of withholding tax on interest on securities issued by the Central and States Government to a resident non-corporate assessee has been reduced from the current rate of 20% to 10%.

Tax assessment

The Finance Bill 2008 has proposed the following:

1. To advance the filing date of income tax and fringe benefit tax returns for corporate assesseees to 30 September.
2. To enlarge the power of the Assessing Officer to suo moto extend the period for the completion of a special audit and empower the Assessing Officer to make certain adjustments on account of arithmetical error or incorrect claims.
3. The notice for initiation of scrutiny assessment be issued within six months from the end of the financial year in which a return is submitted.

4. To allow the Assessing Officer to initiate reassessment proceedings even where the assessment order is a subject matter of appeal/reference/revision. However, this power can be exercised only in respect of those items of income which are specifically not the subject matter of appeal/reference/revision.
5. The participation of an assessee in tax proceedings would prevent the assessee from pleading that the notice for assessment was not served properly or served after the due date.

Penalty

A direction to initiate penalty proceedings while framing assessment would constitute sufficient satisfaction for initiation of such proceedings. A new scheme of waiver of penalty and immunity from prosecution has been proposed to be introduced for cases where the settlement application of the assessee abates.

Tax appeals

It has been proposed that Tribunal's power to grant stay of demand be curtailed to 365 days even if the appeal could not be disposed of for reasons not attributable to the assessee. The Central Board of Direct Taxes is directed to lay down guidelines for regulating filing of appeals by the income-tax department. However, non-filing of appeals pursuant to such guidelines will not prevent the income-tax department from filing appeals for the same assessee's case for other assessment years and for other assessees for the same year or other years.

Fringe Benefit Tax (FBT)

It is proposed that the FBT recovered from the employees on account of shares allotted under employee share option plans shall be deemed as income-tax paid by such employees in relation to the value of such fringe benefit provided to them.

The following expenditures are proposed to be excluded from FBT:

1. Prepaid non-transferable electronic meal card which is usable only at eating joints and outlets subject to other conditions as may be prescribed.
2. Providing crèche facility for children of employee.
3. Sponsoring an employee sportsman.
4. Organizing sports events for employees.
5. Maintenance of accommodation in the nature of guest house.

Value of fringe benefit on account of expenditure on festival celebrations is proposed to be reduced from the existing rate of 50% to 20%.

Banking Cash Transaction Tax (BCTT)

It is proposed to discontinue BCTT after 31 March 2009.

Securities Transaction Tax (STT)

The Finance Bill 2008 proposed to broaden the scope of STT on sale of options and futures in securities with effect from 1 June 2008.

Commodities Transaction Tax (CTT)

A new tax called CTT has been introduced. CTT is applicable on taxable commodities transaction entered in a recognised association. Taxable commodities transaction has been defined as transaction of purchase or sale in a recognised association of option in goods or commodities derivatives and any other commodity derivative.

The amount of CTT paid by the assessee during the course of business shall be allowed as deduction, provided that income from such transaction in commodities is considered as business income.

INDIRECT TAXES

As per the Finance Minister, there has been considerable progress in preparing a roadmap for the introduction of the goods and services tax (GST) with effect from 1 April 2010. As a step forward, the rate of central sales tax (CST) is proposed to be reduced to 2% from 1 April 2008. The general rate of central value added tax (CENVAT) has been reduced from 16% to 14% for all goods. The other ad-valorem rates of 24%, 12% and 8% have been retained.

Customs Duty

The Budget 2008 has maintained the peak rate of basic customs duty (BCD) on all non-agricultural products at 10%. Customs duties have however been reduced in relation to specific industries.

The duty on project imports has been reduced from 7.5% to 5%. However, additional duty of customs in lieu of sales tax/value added tax (VAT) at 4% has been imposed on power generation projects (other than mega power projects), transmission, sub-transmission and distribution projects and goods for high voltage transmission projects.

A Countervailing Duty (CVD) of 1% has been levied on mobile phones.

Further, BCD on certain specified items such as helicopter simulators, specified parts of set top boxes, raw material used in information technology (IT)/electronic hardware industry, ground equipment for testing of satellites and payloads, etc. has been exempt.

BCD has been reduced on certain life saving drugs, convergence products, specified raw materials for tyre industry, specified machinery for manufacture of sports goods, crude & unrefined sulphur and certain specified metal scraps.

Excise Duty

The general rate of CENVAT has been reduced from 16% to 14%.

The CENVAT on various goods like cars, writing paper, printing paper and packing paper, drugs and pharmaceuticals, water filtration and purification devices, pan masala not containing tobacco, etc. have been reduced.

Further, various goods like anti AIDS drugs and bulk drugs, packaged tender coconut water, tea and coffee mixes, specified refrigeration equipment, etc. have been exempt from excise duty.

The duty on packaged software has been increased from 8% to 12%.

National Calamity and Contingent Duty at the rate of 1% has been imposed on mobile phones.

Rule 6 of the CENVAT Credit Rules, 2004 has been amended to provide an option for reversal of credit attributable to common inputs or input services used in relation to the manufacture of both dutiable and exempt goods subject to the procedure mentioned in the said rule.

The rate of duty applicable to clearance of goods to Domestic Tariff Area from 100% export oriented units has been revised from “25% of BCD plus excise duty payable on like goods” to “50% of BCD plus excise duty payable on like goods”.

Service Tax

The rate of service tax remains to be at 12%. However, the composition rate for works contract services has been increased from 2% to 4%.

The threshold limit of service tax exemption for small service providers is being increased from the present level of INR8 lakhs to INR10 lakhs. Consequently, the limit for obtaining service tax registration has also been increased to INR9 lakhs.

The following new categories of services have been brought within the tax net:

1. Services provided in relation to IT software for use in the course or furtherance of business or commerce (such as software development, upgrade including right to use IT software for commercial exploitation and IT software supplied electronically).
2. Asset management services under unit-linked insurance business plans.
3. Services of a recognised stock exchange in relation to securities.
4. Services of a recognised association or a registered association in relation to sale or purchase of any goods or forward contracts.
5. Services of a processing and clearing house in relation to processing, clearing and settlement transactions in securities, goods or forward contracts.
6. Services in relation to transfer of right to use tangible goods not chargeable to sales tax/VAT (such as charter hire of vessels and equipment).
7. Internet telecommunication services (the previous category of internet telephony services has been replaced by this category).

The scope of some existing categories of taxable services has been amended as follows:

1. To include:
 - (1) Purchase or sale of foreign currency, including money changing, by an authorised dealer or an authorised money changer, under banking and other financial services and also under foreign exchange broker services provided by individuals.
 - (2) Packing, together with transportation of cargo or goods, under cargo handling service.
 - (3) Testing or analysis of IT software under technical testing and analysis service.
 - (4) Inspection, examination and certification of IT software under technical inspection and certification service.
 - (5) Services provided in relation to a journey from one place to another in a contract carriage vehicle, under tour operator service.

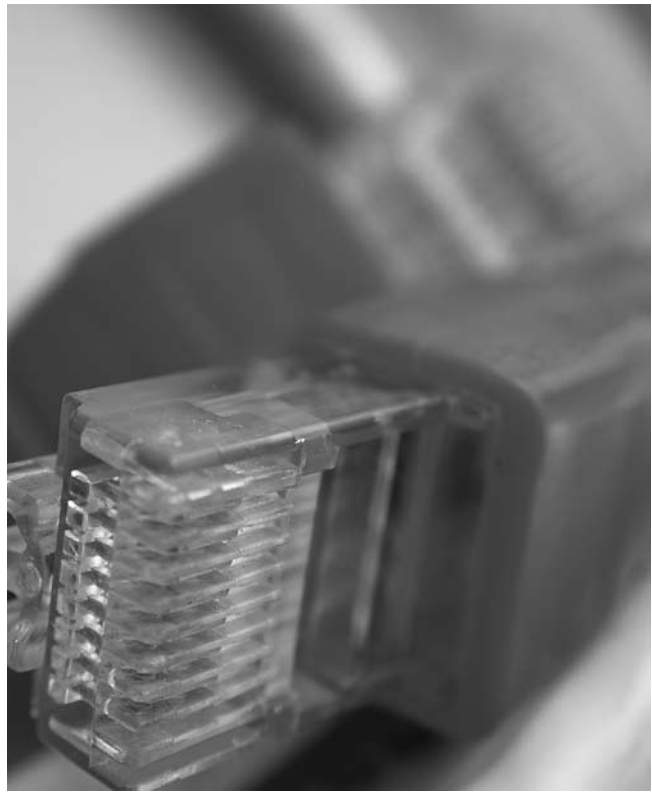
2. To exclude:

- (1) From business auxiliary service, reference to IT service consequent upon notifying IT software service as a separate taxable service.
- (2) From consulting engineer service, reference to computer software engineering consultancy consequent upon notifying IT software service as a separate taxable service.
- (3) From 39 specified taxable services, references to service recipient as "client" or "customer" and replacement thereof with the words "any person".

The Export of Services Rules, 2005 have been modified with effect from 1 March 2008 to grant the benefit of exports to certain services, provided remotely through the internet or any electronic network, including a computer network in relation to goods or materials or any immovable property situated outside India at the time of provision of service. Parallely, an amendment has been made in the Taxation of Services (Provided from Outside India and Received in India) Rules, 2006 with effect from 1 March 2008 to tax similar services under the reverse charge mechanism.

The CENVAT Credit Rules, 2004 are being amended to:

1. Exclude goods transport agency service from the scope of "output service".
2. Allow removal of capital goods outside the premises of the provider of output services, without restriction, for providing output services.
3. Provide the following options to a provider of both taxable and exempt output services, i.e., either using common inputs or input services and opting not to maintain separate accounts or reversing the credit attributable to the inputs and input services used for providing exempt service, to be worked out in a manner prescribed in the rules.
4. Prescribe a procedure to enable the provider of output services to take credit on inputs and capital goods on the basis of an invoice/challan/bill issued by its other office.



RECENT LEGISLATIVE CHANGES CONCERNING TAX TREATIES

1. India and Mexico has signed Double Taxation Avoidance Agreement (DTAA) in September 2007.
2. The Union Cabinet has given approval for signing of the DTAA with Tajikistan and Luxembourg.
3. DTAA between India and Kuwait came into effect from 1 April 2008.
4. The amendment to DTAA between India and the United Arab Emirates was effective from 1 April 2008. The major amendments are:
 - (1) The definition of "Resident" has been changed.
 - (2) The capital gains arising from the alienation of the shares of a resident company will be taxed in the country where the company is resident.