Grant Thornton

Union Budget 2009-10

IT/ITES Industry

A Run-Up

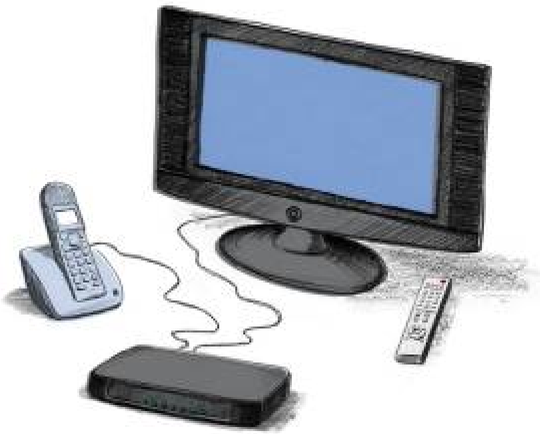
In its latest industry update in March 2009, NASSCOM , India's premier IT (information technology) / ITES (IT enabled services) association that represents and sets the tone for public policy for Indian IT / ITES companies forecasted that the Indian IT / ITES industry would continue to be India's growth engine; contributing about 5.4% to India's GDP.

The industry continues to provide direct employment to 2 million people and generates four million additional indirect jobs related to it and expected to grow by about 16-17% during FY 2008-09 (US$47 billion).

The IT / ITES exports continue to constitute over 65% of the aggregate industry (US – 68% & Europe – 51%) and is therefore most vulnerable to the deepening global economic downturn (world growth is expected to fall 0.5% in 2009 and recover by 3% in 2010).

The IT / ITES industry including hardware is expected to clock about US$72 billion for FY 2008-09 with the domestic market accounting for only about US$ 12.5 billion.

NASSCOM acknowledges that the global technology spend is expected to reduce in the first two quarters of 2009 on account of the global downturn and expects it to pick up in 2010.



Key Expectations

Policy measures

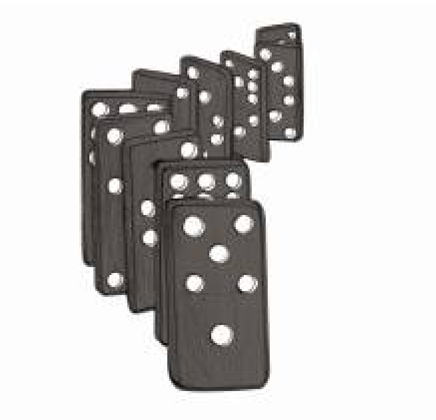
- The Government ought to stimulate and encourage IP (intellectual property) creation in India
- Government should accelerate spending of funds allocated to IT (information technology) & other growth oriented measures to stimulate the domestic market
- Government should provide sops for improving the quality of education and skill building
- Stable policy regime for the IT hardware industry
- Improved Infrastructure facilities- Roads, power, airports

Direct Tax

- Extension of the income-tax holiday to STPI (Software Technology Parks of India) / EOU (export oriented unit) schemes by 3 to 5 more years given the global economic slowdown
- Rationalisation of Transfer Pricing Provisions especially limiting the deeming fiction in the definition of 'associated enterprises' and penalty provisions

Indirect Tax

- Rationalisation of customs duty on imported equipments
- Removal of 4% Special Additional Duty (SAD) in line with phase out of central sales tax (CST)
- Increase permissible abatement from about 22% to 35% under excise for MRP based products
- Clarification of the legal position in respect of packaged or customised software for taxability under service tax, excise and VAT



Direct Tax Proposals

- Sun-set clauses for deduction in respect of export profits under sections **10A and 10B** of the Income Tax Act being extended by one more year i.e., for the financial year **2010-11**

- **FBT abolished** to avoid the compliance burden on assessee
  - Assessment period (u/s 115WE) extended by one more year

- **SEZ 10AA**- With effect from AY 2010-11, deduction formula would now consider the total turnover of the "**undertaking**" and not that of the 'assessee'

- Changes to **MAT** provisions:
  - Increase from **10% to 15%**
  - Credit carry-forward extended from **7 to 10 years**
  - **Provision** for any diminution in the *value of any asset* to be added back for computation of book Profit

- **Deduction in Computing Total Income**
  - Aggregate deduction limit of **10A, 10AA, 10B and 10BA** companies would be limited to the profits and gains of the undertaking
  - Claim necessarily to be made in Return of Income
  - **Inter-unit transfer** of goods or services to be **at market value**

Transfer Pricing

- Amendment relating to **clarification** on calculation of **+/-5% range**

- Introduction of "**safe harbour**" rules – CBDT to formulate rules effective April 1, 2009

- Proposal for constitution of **dispute resolution panel** for TP-related variations arising from assessments

Indirect Tax Proposals

- Exemption granted from excise duty and countervailing duty on packaged software on value representing consideration for transfer of the right to use such software

Expert Viewpoint

Direct tax

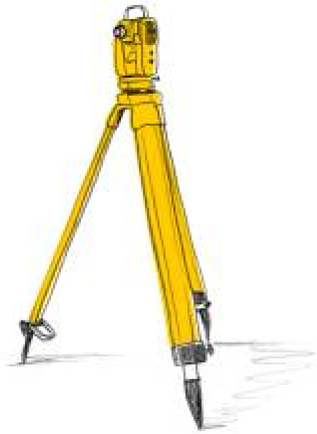
- **Deduction formula** for Section 10AA benefit has **not been amended with retrospective effect**. SEZ tax holiday benefit for the past years may continue to be computed in a manner disadvantageous to the assessee

Indirect Taxes

- The **ambiguity** on applicability of service tax and VAT on **packaged and customised software continues** could cause litigation
- No other major expectation fulfilled by Budget 2009

Transfer Pricing

- **Safe harbour** provisions would give a breather to the **Captive IT-ITeS** companies which suffered major TP adjustments
- Proposal for setting-up separate **dispute resolution forum for TP related cases** is another welcome step which **would help speedy resolution of disputes**



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