Grant Thornton

Union Budget 2009-10

Pharmaceuticals

The most significant aspect of the Indian Pharmaceutical industry is that India is now the fifth largest producer of drugs and pharmaceutical after USA, Japan, Europe and China

Domestic pharma market, which consistently grew at 9.5% CAGR in last 5 years, is poised to accelerate at 13.6% between 2006-10 to touch the market size of US$ 9.48 billion by 2010 from present level of little over US$ 5.7 billion, according to a Paper brought out by The Associated Chambers of Commerce and Industry of India (ASSOCHAM) and Cygnus

The following factors would trigger the growth of the industry:

- India's large population in an untapped market with huge potential
- Low cost of production
- Efficient technologies for large number of generics
- Large pool of skilled technical manpower

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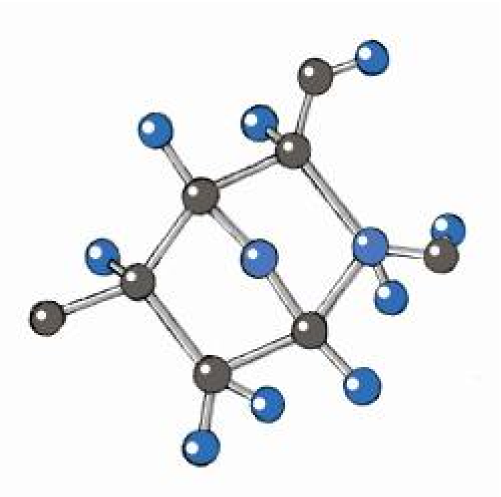
The following factors could hinder the growth of the industry:

- Large amount of price regulation
- Large amount of small players increases price competition and decreases efficiency of the industry as a whole
- Lack of product patent
- Fragmentation of the Indian pharmaceutical industry



Key Expectations

Income Tax

- Incentives to be provided for R&D (Research and Development) activities by reintroducing tax incentives under section 80IA / 80IB of the I-T Act (Income tax Act)
- Extend benefit of tax holiday under section 10A / 10B to units engaged in export of healthcare related services
- Continuation of the tax shelter in specified zones like Himachal Pradesh, Sikkim and Jammu
- Exclude expenses on conferences of doctors and sales personnel from the ambit of FBT (Fringe Benefit Tax)

Customs Duty

- Exemption of custom duty for import of all capital goods, inputs, consumables and reference standards for R&D purposes
- Extension of customs duty exemption to more life saving drugs and other anti–Aids and anti–cancer formulations

Excise Duty

- Uniformity in excise duty rates on active pharmaceutical ingredients (APIs) and formulations by reducing the excise duty on APIs
- Goods manufactured in R&D centres should be exempted from excise duty and service tax
- Extension of excise duty exemption to more life saving drugs and other anti – Aids and anti – cancer formulations

Others

- Strengthen and increase capital outlay for academic institutions engaged in scientific research
- Requirement of a single window clearances instead of multiple clearances from different institutions for testing a new molecule
- Passing of Central Drug Authority Bill – pending for the last five years
- Removal of cost based price controls
- Introduction of Unified GST (Goods and Services Tax)

Key Expectations

Incentives for undertaking R& D activities

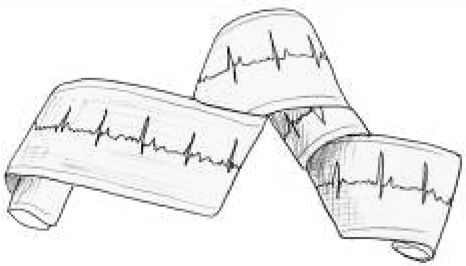
Benefit of 10A/10B for exports

Tax shelter in Himachal Pradesh, Jammu and Sikkim

Customs / Excise duty exemption for life saving drugs

Removal of cost based price controls

Introduction of unified GST



Direct Tax Proposals

- Extension of benefits under section 10A and 10B of the Income Tax Act by one more year i.e. for financial year 2010-11. However, the term "manufacture" is now defined under the Act and therefore the eligibility of companies engaged in contract research to qualify for exemptions under Section 10A / 10B is unlikely
- Benefit of weighted deduction of 150% on expenditure incurred on in-house R&D extended to all manufacturing business
- With effect from 01 April 2009, tax benefit under section 10AA to be computed taking "total turnover of the undertaking" as the denominator instead of "total turnover of the business of the assessee". This much awaited amendment however is not retrospective in nature
- Minimum Alternate Tax (MAT) to be increased to 15% of book profits from 10 % and carry forward of tax credit under MAT extended from 7 years to 10 years
- Tax Deduction at Source (TDS) rate would be 20% in case the deductee does not furnish the valid Permanent Account Number
- Abolition of Fringe Benefit Tax (FBT)
- Amendment relating to clarification on calculation of +/- 5% range under the transfer pricing regulations
- Introduction of "safe harbour" rules – CBDT to formulate rules effective 01 April 2009
- Setting up of an Alternate Dispute Resolution Panel to achieve speedy and efficient disposal of transfer pricing cases

Amendments

Benefits of 10A/10B extended for one more year

Fringe Benefit Tax abolished

Minimum Alternate Tax increased to 15%

SEZ formulae anomaly rectified; however prospectively

Introduction of Alternate Dispute Resolution Panel and safe harbour norms under transfer pricing regulations

Indirect Tax Proposals

The following changes in duty rate have been introduced in the Budget 2009:

Customs Duty

Product	New rate	Old rate
Additional Life Saving drugs such as Abatacept, Daptomycin, Influenza Vaccine, etc.	5%	10%
Artificial Heart	5%	7.5%
Medical devices – Patent Ductus Arterious/ Artial Septal Defect Occulusion	5%	7.5%

Excise Duty

Product	New rate	Old rate
Medical devices – Patent Ductus Arterious/ Artial Septal Defect Occulusion	NIL	14%
Contact Lenses	8%	4%

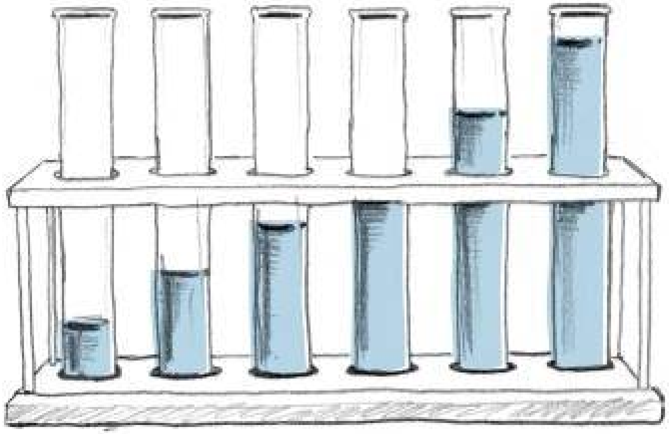
Indirect Tax Proposals

- Excise duty on goods attracting 4% has been increased and rationalized to 8%. However, drugs and pharmaceutical products and medical equipments continue to attract 4% rate of duty

- Small Scale Industry (SSI) exemption scheme under the Central Excise is extended to manufacturers of printed laminated rolls bearing the brand names of others who have crossed the SSI turnover

- Cosmetic and Plastic Surgery Services proposed to be brought under the service tax net from a date to be notified after enactment of the Finance Bill, 2009. Non invasive plastic surgery is also proposed to be taxed. However surgery undertaken to restore/reconstruct anatomy or functions of the body affected due to congenital defects, diseases, injury or trauma will not be taxable

- The ambit of business auxiliary services has been amended to exclude from the levy only those activities on which Central Excise duty is payable. Certain pharmaceutical industries that use potable alcohol and are subject to state excise would be affected by this amendment



Expert Viewpoint

- Extension of 10A / 10B for an additional year is in line with industry expectations. This will boost the spirits of pharma companies availing of such benefits for export of specific healthcare related services

- Abolition of FBT will enable pharma companies to save on tax outgoings pertaining to FBT, which was earlier leviable on sales promotion activities

- Transfer Pricing which has been one of the foremost concerns for this industry may see some relief in terms of faster disposal of cases through the introduction of an Alternate Dispute Resolution Panel

- Duty on additional life saving drugs and specified medical equipments has been reduced and the lowest rate of 4% excise duty maintained for pharmaceutical products

- The Pharma industry will benefit from the extension of SSI exemption scheme granted to manufacturers of printed laminated rolls bearing their brand names being an input for packing of pharma products

- Non-resident companies licensing IPRs to Indian pharma companies may be subject to a higher TDS rate at 20% in case of non-availability of a Permanent Account Number. The lower rate of 10.5575% under domestic law may no longer be available

- The expectation of rationalization of duty on raw material to converge with international standard has not been given its due importance

- The date of 1st April,2010 being fixed for the introduction of GST is a welcome development for the pharma sector

Our Offices

BANGALORE
3274/A, 11th Main
HAL 2nd Stage
Indiranagar
Bangalore 560 008

CHANDIGARH
SCO 17
2nd Floor
Sector 17 E
Chandigarh 160 017

CHENNAI
Unit nos. 13, 14 and 16 11,
Thiru-vi-ka Rd
Royapettah
Chennai 600 014

GURGAON
Centre Point
3rd Floor
Sushant Lok, Phase I
Gurgaon 122 002

HYDERABAD
Uptown Banjara
Road No 3
Banjarahills
Hyderabad 500 034

MUMBAI
Engineering Centre, 6th
Floor, 9, Matthew Road
Opera House
Mumbai 400 004

NEW DELHI
National Office
Outer Circle
L 41, Connaught Circus
New Delhi 110 001

PUNE
401, Century Arcade
Narangi Baug Road
Off Boat Club Road
Pune 411 001

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