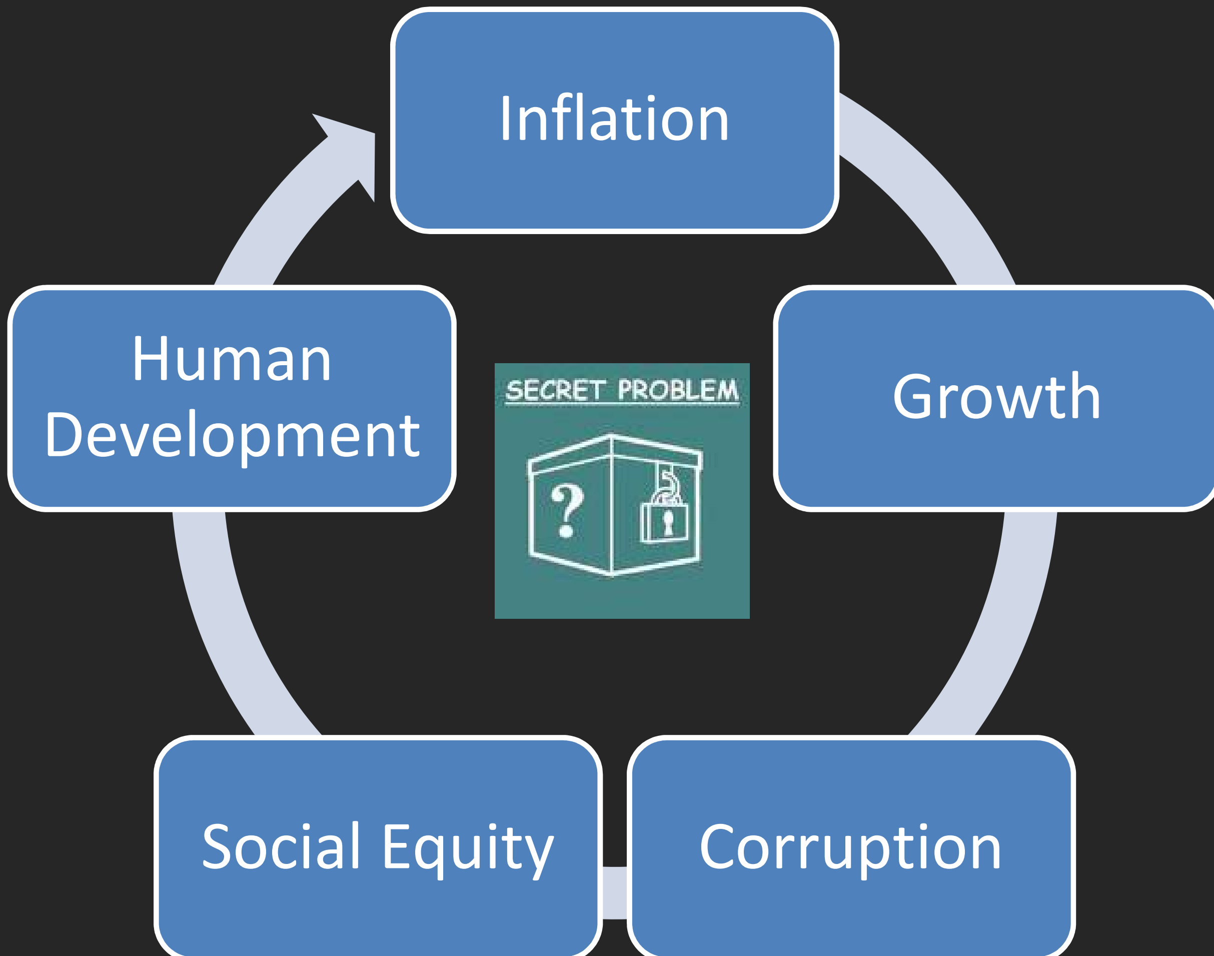
Union Budget 2011

"It's clearly a budget. It's got a lot of numbers"

1st March 2011

The Perennial Conundrum



The Budget Imperatives & the Govt. Response

Imperative	Response
Control Inflation	Removal of 140 exemptions in Central Excise
Eradicate Corruption	Wide powers under Service Tax
Stimulate Growth	Adverse Income Tax Implications for SEZs
Create Balanced Growth	Service Tax on Education, no tax on film actors
Develop Human Capital	Avoid air-conditioning since it is a luxury

The numbers in the Budget…

- Proposals relating to Service Tax estimated to result in net revenue gain of Rs. 4,000 crore.

- No increase in tax rate. Only 2 new services introduced.

- Are we missing something?
  - The devil is in the details….

So what are the details…

- With a plan to introduce GST,
  - 140 Central Excise exemptions withdrawn
  - Service Tax moved to Accrual Concept
- Are we really close to GST?
- Do we send the right signals?

Let’s compare

Principles of GST	How Violated
Uniformity of Taxation	Software – Liable for Central Excise, Service Tax, VAT, Customs, Octroi ???
Unfettered Input Credit	No Credit for Employee Costs No Credit for Construction Costs Sectoral Credit Restrictions Partial Credit Loss for Investments Credit Loss for Trading Credit Loss for Concessional Excise Rate
Singular Rate	Excise has 0 – 1 – 5 – 10 (over and above ad hoc amounts) Service Tax has 0 – 0.10 – 0.60 – 1.20 – 2.50 – 3.30 - 4.00 -5.00 – 6.00 – 7.50 – 10 (over and above ad hoc amounts)

Budget at a Glance

- Service Tax
- Central Excise Duty
- Customs Duty
- Income Tax

Payment of Tax

- Service Tax to be paid on the basis of point of provision of service instead of receipt of service
- Point of Taxation Rules introduced to define provision of service
  - In general, the point is the provision of service or receipt of money or raising of invoice whichever is earlier
- Suo Motu Adjustment Limit increased from Rs. 1 lakhs to Rs. 2 lakhs

Payment of Tax: Issues

- What happens in cases where the invoices are subject to certification and approval?
- What happens if lesser amount is realised?
- What happens if the amount is not realised?
- What happens if service is not provided subsequently?
- When can CENVAT be claimed by the service recipient?

Payment of Tax: Transitory Aspects

- When will the amended provisions come into effect?
- What would be the status of invoices raised but not realised as on the cut off date?
- How will the exemption for small service providers work in this case?
- How to deal with special cases in defining point of taxation?

Point of Taxation Rules:
Is it a point or a circle of infinite possibilities?

Situation	Point of Taxation
General	Date of Provision of Service, Invoice or Receipt whichever is earlier
Import of Services	Date of Invoice or Remittance whichever is earlier
Continuous Service	Date of Milestone, Invoice or Receipt whichever is earlier
Associated Enterprises	Date of Entry in Accounts, Invoice or Receipt whichever is earlier
Intellectual Properties	Each time the amount is determined based on usage by the service recipient

What's brewing in the POT ?

Special Situation	Point of Taxation
Intermediary Change in Tax Rate	Endless Possibilities, some addressed some not.
Introduction of New Service:	
• Services Provided before the effective date	Not Taxable, subject to Rule 4A Compliance
• Payment Received before the effective date	Not Taxable, subject to Rule 4A Compliance
• Invoice Raised before the effective date	Not specifically addressed, but seems to be taxable

Interest

Provision	Amendment
Interest on delayed payment of service tax	Interest Rate increased from 13% per annum to 18% per annum
Interest on delayed payment of amount collected in lieu of service tax	Interest Rate increased from 13% per annum to 18% per annum
Interest in case of small assessees having value of taxable services < 60 lakhs in preceding financial year	Lower Interest Rate of 15% per annum

SCN: Current Provisions: Recipe for Sleepless Nights

- Substantial Ambiguity in Taxation
- Investigation culminating in SCN
  - Tax on Gross Receipts for last 5 years
  - Interest
  - Penalties
- High Pitched Assessments at times exceeding the gross receipts
- Introduction of concept of "Captured Transactions"

Penalties for delayed payment of tax

- Penalties reduced to half
  - Still high @ 100 per day or 1% per month restricted to 50% of the tax due
- Whether penalties under section 76 can be waived if penalties imposed under section 78?

Penalties for Suppression

Situation	Quantum of Penalty	Whether can be waived?
Fraud, Collusion, Wilful Mis-statement, Suppression, Intentional Contravention	100% of the Service Tax Amount	Not Subject to Reasonable Cause
Captured Transactions	50% of the Service Tax Amount	Subject to Reasonable Cause
Amt. Paid within 30/90 days of the Order in Original	25% of the Service Tax Amount	Penalty voluntarily paid
Amt. Paid before SCN for Captured Transactions	1% per month of the Service Tax Amount restricted to max. of 25% of the Service Tax Amount	Not subject to reasonable cause

Other Penalties

Provision	Current Penalty	Proposed Penalty
Late Filing of Service Tax Returns	Upto Rs. 2,000/-	Upto Rs. 20,000/-
Failure to take Registration	Rs. 5000/- or Rs.200 per day whichever is higher	Rs. 10,000/- or Rs.200 per day whichever is higher
Failure to maintain books of accounts or documents	Upto Rs. 5000/-	Upto Rs. 10,000/-
Failure to furnish information/produce documents/respond to summons for personal attendance	Rs. 5000/- or Rs.200 per day whichever is higher	Rs. 10,000/- or Rs.200 per day whichever is higher
Payment by normal banking channel though liable to pay by electronic mode	Upto Rs. 5000/-	Upto Rs. 10,000/-
Issue of Incorrect/ Incomplete Invoice or Failure to Account for the Invoice in Books of Accounts	Rs. 5000/-	Rs. 10,000/-
Any other non-compliance/contravention	Rs. 5000/-	Rs. 10,000/-

Prosecution - Scope

- Provides any taxable service without a valid invoice
  - Receives any imported service without a valid invoice
- Avails and utilises credit of taxes without actual receipt of service/ goods
- Maintains false books of account or fails to supply any information or supplies false information
- Collects any amount as service tax but fails to pay the amount within six months

Prosecution - Term

Situation	Minimum Term	Maximum Term
Amount exceeding 50 lakhs	6 months	3 years
Others	--	1 year
Subsequent Offence	6 months	3 years

- No Lame Excuses like
  - First Time Offence
  - Penalty or other damages
  - Not Principal Offender
  - Age of the Accused

CENVAT Credit : Story so far

- Credit granted to avoid cascading effect of taxation
- Problems in composite cases
- However, the scars of “post removal” & “nexus” are too big
- At the same time, the urge to monetize is equally alluring
- Various issues sought to be addressed by this Budget

Re-Emergence of “Nexus”

- Removal of Phrase “Activities Relating to Business” from the definition of input services
- Nexus presumed to be absent in case of
  - Employee Related Costs
  - Motor Vehicle Related Costs
  - Civil Work
- Systems to capture CENVAT Credit will need a thorough review

CENVAT Eligibility Criteria

Nature of Input	Eligibility
Goods used in the factory by manufacturer	Yes
Goods cleared with finished goods as accessories	Yes
Goods used for providing free warranty for excisable goods	Yes
Goods used for generation of electricity	Yes
Goods used for providing output service	Yes
LDO/HSD/Motor Spirit	No
Goods used for construction of building or civil structure or foundation for capital goods	No, except for port, airport, construction, works contract service providers
Capital Goods	No, except when used as parts or components
Motor Vehicles	No
Goods for consumption of employee	No
Goods with no relationship to manufacture	No

CENVAT Eligibility Criteria, Available Credits

Nature of Input Service	Eligibility
Services used for providing output service	Yes
Services used in relation to manufacture of final goods	Yes
Modernisation, Repairs or Renovation of Premises	Yes
Advertisement, Sales Promotion, Market Research, Storage, Procurement of Inputs, Accounting, Auditing, Financing, Recruitment and Quality Control, Coaching and Training, Computer Networking, Credit Rating, Share Registry, Security, Business Exhibition, Legal Services	Yes

CENVAT Eligibility Criteria
Negative List

Nature of Input Service	Eligibility
Architect, Port, Airport, Construction & Works Contract Services used for construction	No, unless used for providing specified output services
Insurance, Rent a Cab, Repairs or Supply of Tangible Goods Services connected with motor vehicles	No, unless the credit is available on the motor vehicle itself
Outdoor Catering, Beauty Treatment, Health Services, Cosmetic Surgery, Club, Health Club. Life Insurance, Health Insurance, Travel Benefits to employees	No

CENVAT & Civil Construction

Nature of Transaction	Eligibility	Further Restrictions, if any
Goods used for construction of building or civil structure or foundation for capital goods (In General)	No	N.A.
Goods used for construction of building or civil structure or foundation for capital goods (for port, airport, construction, works contract service providers)	Yes, if service tax paid on full value including materials	Service Tax not eligible as credit to the manufacturer
Architect, Port, Airport, Construction & Works Contract Services used for construction (In General)	No	N.A.
Architect, Port, Airport, Construction & Works Contract Services used for construction (For Contractors)	Yes	Credit restricted to 40% if ED Credit claimed by subcontractor

CENVAT : Restrictions on Availment

- No credit eligible for goods cleared under concessional rate of 1%
- Existing CENVAT cannot be utilised for payment of concessional rate of 1%
- Credit of ADC restricted to 85% in case of ships, boats & other floating structures
- Reversal of Credit on input services if the payment is refunded.

CENVAT : Composite Output

Nature of Transaction	Taxable	Exempted
Manufacture of Excisable Goods	Yes	No
Manufacture of Exempted Goods	No	Yes
Manufacture of Goods cleared at 1% Rate	No	Yes
Clearances to SEZ Units/Developers	Yes	No
Export of Goods and Services	Yes	No
Provision of Taxable Services	Yes	No
Provision of Exempted Services	No	Yes
Services on which Abatement is claimed under Notification 1/2006-ST	No	Yes, to the extent of abated value
Services on which Composition Scheme /Special Rates Availed	Yes, value corresponding to tax amount	No
Trading in Goods	No	Yes, to the extent of gross profits
Services to SEZ Units/Developers	Yes	No
TOTAL SAY	1,00,00,000 ~ 40%	1,50,00,000 ~ 60%

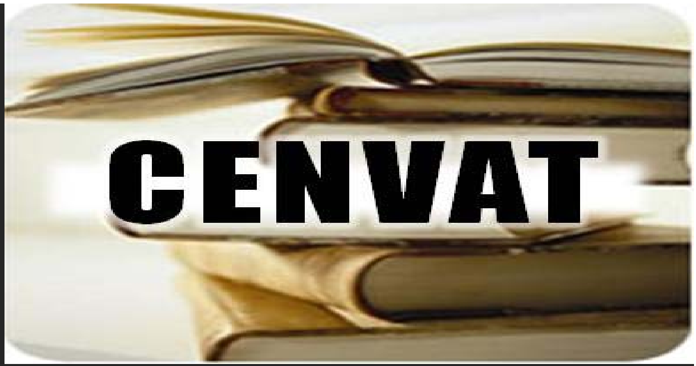
CENVAT : Composite Output

	Total	Credit Available
Specific Identification and claim for taxable goods / services (Option I)	2,00,000 Say 1,10,000 + 90,000	Claim 1,10,000
No identification – composite scheme for manufacturers / service providers based on output (ad hoc payment) – OPTION II	2,00,000	Claim 2,00,000 Pay 7,50,000
No identification – composite scheme for manufacturers / service providers based on input & input services (proportionate payment) – OPTION III	2,00,000	Claim 2,00,000 Pay 1,20,000
No identification – composite scheme for manufacturers / service providers based on input services (proportionate payment) – OPTION IV	2,00,000 Say 60,000 + 20,000 + 1,20,000	Claim 60,000 + 1,20,000 Pay 72,000

CENVAT: Common Points

- *Provision granting FULL Credit for specified services is deleted*
- *FULL Credit available for capital goods if used for common purposes*

CENVAT: Special Cases



Nature of Service	Special Payments
Banking & Financial Services provided by banking company, financial institution or NBFC	Pay 50% of the amount claimed as credit on input and input services
Services in the nature of life insurance and ULIP Related Services	Pay 20% of the amount claimed as credit on input and input services

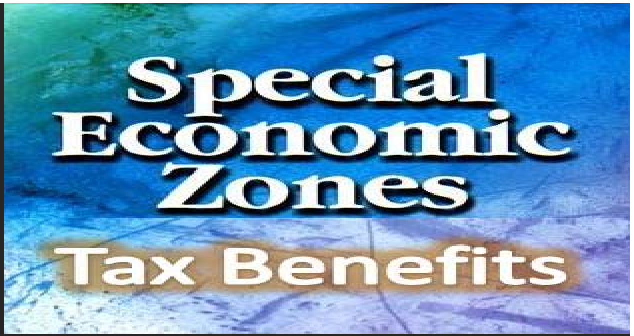
Export/Import of Services: A Game of Basket Ball?

Category of Service	Earlier Basket	New Basket
Builder Related Services	Recipient Based	Property Based
Rail Travel Agent	Recipient Based	Performance Based
Health Related Services	Recipient Based	Performance Based
Credit Rating Agency	Performance Based	Recipient Based
Market Research Agency	Performance Based	Recipient Based
Technical Testing and Analysis	Performance Based	Recipient Based
Air Transport Services	Performance Based	Recipient Based
Goods Transport Agency Services	Performance Based	Recipient Based
Opinion Poll Services	Performance Based	Recipient Based
Rail Transport Services	Performance Based	Recipient Based

Transport & Logistics: Ankle Sprain?

Category of Service	Service Tax Implication
Transport of Goods by Road for trans-shipment	Exempt vide Notification 8/2011
Transport of Goods by Rail for trans-shipment	Exempt vide Notification 8/2011
Transport of Goods by Air for trans-shipment	Exempt vide Notification 8/2011
Transport of Goods by Water for trans-shipment	Not needed in view of the definition set
Other Services (eg. Port Services) for trans-shipment	Taxable
Transport of Goods by Air where airfreight included in customs valuation	Exempt vide Notification 9/2011
Transport of Goods by Water (General)	Abatement provided to the extent of 25% of the value. Effective Service Tax Rate @ 7.725%

SEZ Units/Developers



- Clarity on eligibility of ST, EC & SHEC
- Present scheme to continue but exemption for services consumed within SEZ will be optional
- Consumption linked with Place of Supply Rules
  - Recipient – does not own or carry on any business other than operations in SEZ
- Approved list of Authorised Operations
- Declaration in Form A-1

SEZ Units/Developers – Service Provider Perspective

Nature of Service	Whether exempt/taxable	Documentation Required for Exemption	Whether corresponding CENVAT Available
Property Related Services on SEZ located property	Optionally Exempt	List of Authorised Operations	Yes
Performance Related Services wholly performed within the	Optionally Exempt	List of Authorised Operations	Yes
Recipient Based Services provided to SEZ not having any other business	Optionally Exempt	List of Authorised Operations Form A-1 bearing the name of service provider	Yes
Other Cases	Taxable	N.A.	N.A.

SEZ Units/Developers – Service Recipient Perspective

Nature of Service	Eligibility for Refund
Wholly consumed	Full
Partly consumed	Proportionate

Introduction of New Services

- 2 new services introduced
  - AC Restaurants-cum-bars
  - Hotel Accommodation
- Effective from a date to be notified after enactment
- Impact of Point of Taxation Rules

AC Restaurants-cum-bars

- Requirements for levy of Service Tax
  - Air Conditioned
  - License to Serve Liquor
- Following not covered
  - Mere Sale of Food (Pick up or Home Delivery)
  - Goods Sold at MRP
- Abatement @ 70% of the Gross Bill Amount to be provided at the time of enactment
- Effective Service Tax Rate @ 3.09% of the gross value

Service Tax on AC Restaurants cum bars (Issues)

- Is there an element of service?
- Does it overlap with the State Jurisdiction to impose a tax?
- What if the restaurant-cum-bar
  - Is partially airconditioned?
  - Is airconditioned for part of the year?
  - Obtains a license to serve liquor in the middle of the year
- Is VAT payable on the service tax component?

Hotel Accommodation

- What is covered
  - Accommodation provided by Hotel, Inn, Guest House, Club or Campsite
- What is not covered
  - Long Term Stay above 3 months
  - Declared Tariff of Less than Rs. 1000 per day
- Abatement @ 50% of the Gross Bill Amount to be provided at the time of enactment
- Effective Service Tax Rate @ 5.15% of the gross value

Service Tax on Hotel Accommodation: Issues

- Is there an element of service?
- Does it overlap with the State Jurisdiction to impose a tax?
- What if the declared tariff is more than Rs. 1000/- but the actual amount charged is less than Rs. 1000/-
- Is luxury tax payable on the service tax component?
- Is service tax payable on the luxury tax component?

Alteration in Scope of Existing Services

- Scope of Services expanded for the following categories
  - Clinical Establishment Services
  - Commercial Training or Coaching Services
  - Legal Consultancy Services
  - Authorized Service Station
  - Life Insurance Services
  - Clubs or Association Services
  - Business Support Services
- Effective from a date to be notified after enactment
- Impact of Point of Taxation Rules
- Impact on Pending Litigation

Clinical Establishment Services

- What is clinical establishment
  - Hospital satisfying the following conditions:
    - Air conditioning in whole or part of the premises
    - More than 25 beds at any time during the financial year
  - Diagnostic Clinics
  - Doctors (not employees) working in such clinical establishment
- Liability not linked with registration under the Clinical Establishment (Registration and Regulation) Act, 2010
- Excludes Government and municipal hospitals
- Abatement @ 50% of the Gross Bill Amount to be provided at the time of enactment
- Effective Service Tax Rate @ 5.15% of the gross value

Commercial Training or Coaching Services

- Training provided by recognised bodies also covered
- Courses which are recognised will be exempted through a separate notification
- Distinction between training and education whether relevant or diluted

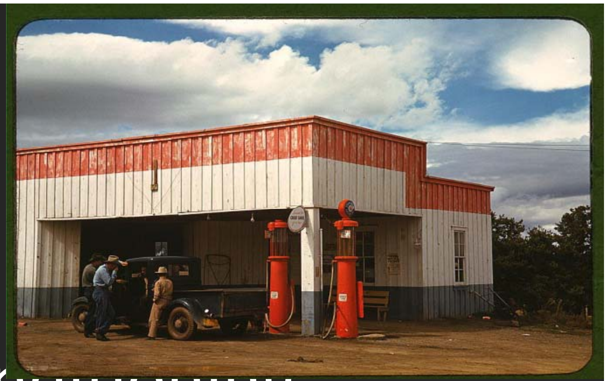
Legal Consultancy Services

- Complex Matrix of Possibilities:

Service Provider	Service Recipient	Nature of Service	covered
Business Entity	Any Person	Advise, Consultancy or Assistance	Yes
Any Person	Business Entity	Representational Services	Yes
Arbitral Tribunal	Business Entity	Arbitration	Yes
Other than Business Entity	Other than Business Entity	Any	No
Other than Business Entity	Any Person	Advise, Consultancy or Assistance	No
Any Person	Other than Business Entity	Representational Services	No

- Exemption provided to Chartered Accountants likely to be withdrawn

Authorized Service Station



- Scope expanded to cover repair, reconditioning, restoration or decoration or any other similar services, of any motor vehicle other than three wheeler scooter auto-rickshaw and motor vehicle meant for goods carriage
- Impact on
  – Other than Authorised Service Stations
  – Authorised Service Stations
- Are repairs of goods carriages still exempt from payment of service tax?

Life Insurance Services

- Components of Life Insurance Premium

Component	Tax Position	Optional Scheme
Risk Cover	Taxed since 10.09.2004	1% of the Total Premium
Investment Component	Not Taxable	Not Taxable
Management of Investment	Already taxed in ULIP Mode	Will be notified as 1.5% of the Total Premium
	Proposed to be taxed for other cases as well	

- Impact under the CENVAT Credit Rules
  - Payment of an amount equivalent to 20% of the Credit availed on inputs and input services

Works Contract Services

Subject Matter	Nature of Amendment	Reference
CENVAT	In case of input services in the nature of construction or ECI services where the tax is discharged on full value, the credit restricted to 40% of the service tax paid	1/2011-ST
JNNURM/RAY	Construction Services provided under 'works contract' mode are exempted	6/2011-ST
Airport	Construction Services provided under 'works contract' mode within an airport are exempted	10/2011-ST
Port	Specified Construction services provided under 'works contract' mode within port are exempted	11/2011-ST

Banking & Financial Services

- Change in Valuation of Taxable Services for money changing activities
  - Difference between the RBI Reference Rate and the transaction rate
- Composition Rate for money changing reduced to 0.1% of the gross amount
- Impact in CENVAT Credit Rules – liability to pay 50% of the credit availed (only for banking companies and financial institutions)

Air Travel Services

Nature of Transport	Originating	Class	Amt. Payable upto 01.04.2011	Amt Payable After 01.04.2011
International Transport	From India	Economy	500 per journey	750 per journey
International Transport	From India	Others	10.30% of gross value	10.30% of gross value
Domestic Transport	From India	Economy	100 per journey	150 per journey
Domestic Transport	From India	Others	100 per journey	10.30% of gross value
International Transport	Outside India	Economy	Not Applicable	Not Liable
International Transport	Outside India	Others	Not Applicable	Not Liable

Other Service Specific Amendments

Category of Service	Nature of Amendment
Clubs or Association Services	Services rendered to non members is also made liable for payment of service tax Associations representing industry or commerce exempt upto 31.03.2008 – eligible for refund as well
Business Support Services	Administrative Assistance also made liable for payment of service tax
Tour Operator	Validation of Retrospective Exemption for point to point transportation – eligible for refund as well
Telecommunication Services	Value shall be the gross amount paid by the subscriber and not the distributor
Business Exhibition Services	Exhibitions outside India exempted from payment of service tax
General Insurance Services	Exemption to services rendered under Rashtriya Swasthya Bima Yojana

Central Excise Duty

- Concessional Rate increased to 5%
- Exempt Items – 1 % rate introduced with no CENVAT, or 5% with optional CENVAT. Some major impact areas include
  - Food Preparations & Beverages
  - RMC
  - Stationery items like envelopes, letter heads, greeting cards, calenders, etc.
  - Branded Jewellery
  - Ships

Central Excise Duty (Contd)

- Branded Readymade Garments liable for excise duty
- Exemption to information technology software for the value representing the consideration for the right to use the software
- Exemption provided for goods required for setting up of Mega and Ultra Mega Power Projects and expansion of mega power projects
- Additional Duties of Excise (Goods of Special Importance)Act , 1957.
- Sugar and textiles are being omitted from the Schedule of the Additional Duties of Excise (Goods of Special Importance)Act , 1957. VAT applicable on Items of Sugar & Textiles effective from 01.04.2011

Other Duties

- Customs Duty
  - No Change in Peak Rate of Duty
  - Self Assessment Procedure Introduced
- Central Sales Tax
  - No Change in the Rate of Tax
  - Change in the maximum chargeable rate in case of declared goods

Income Tax
Rate of Tax

- No change in Income Tax rate
- Basic exemption limit
  - Rs.1,80,000 in general
  - Rs. 1,90,000 for women
  - Rs. 2,50,000 for senior citizens (Above 60 years)
  - Rs. 5,00,000 for very senior citizens (Above 80 years)
- No change in tax rate for firms & companies.
- Reduction in surcharge
  - From 7.5% to 5% in case of Domestic Companies
  - From 2.5% to 2% in case of Foreign Companies

Rate of Tax

- Minimum Alternate Tax
  - On companies raised to 18.50% from 18%
  - also proposed on LLP at the rate of 18%.
- Interest from investment made in infrastructure debt fund eligible for concessional tax rate @ 5%
- Dividend received by Indian Company from its foreign subsidiary eligible for concessional tax rate @ 15%
- SEZ liable to MAT and DDT

Business & Profession

- Weighted Average Deduction of 200% on any contribution made to National Laboratory or University or IIT or specified person
- Additions of 2 new business under Sec 35AD
  - In the nature of developing and building housing project
  - Production of fertilizers

Transfer Pricing

- Variation between ALP and Actual transaction price allowable at the rate notified as against 5% earlier.
- Due Date of filing Report under 3CEB extended to 30th November
- Powers of TPO enhanced.
- Sec 94A – Notified Jurisdictional area
  - Transaction within notified area deemed to be with associate.
  - Authorization to seek information from financial institution.
  - Onus on the assessee to satisfactorily explain the source of money.
  - TDS to be deducted at a higher rate:
    - Rate in force
    - As per Income Tax Act
    - 30%

Deductions

- Contribution made by Central Govt or the employer to pension fund (NPS) shall not be included in 80CCE limit of Rs. 1,00,000.
- 80CCF – Deduction for Contribution to infrastructure bonds (additional amount Rs. 20000) increased by a year.
- Profit& Gain of industrial undertaking – 80IA extended for one more year. (power generation and distribution)
- 80IB – Mineral Oil companies - blocks licensed under a contract awarded after 31.03.2011

Procedural Aspects

- Powers to income tax authority not below level of Assistant Commissioner in case of Agreements of DTAA.
  - Discovery & Inspection
  - Enforcing attendance & examining on oath
  - Compelling production of books of account
  - Issuing commissions
  - Calling for information
- Period of limitation for assessment shall not include period for which reference for exchange of information of Agreements of DTAA.
- Central Govt exempts certain class of persons from requirement of furnishing Return of Income
- Time limit for centralized processing of returns – extended up to 31st March 2012.

Procedural Aspects Cont.

- Cancellation of DIN
- Non – Resident having Liaison office set up in India shall submit statement in prescribed form
- Rectification of order passed by Settlement Commission in case of mistake apparent from record – 6 months
- Similar provisions in Wealth Tax

Thank you