Students may kindly note that the following are the proposals put forth in the Finance Bill 2005. They will come into effect only when the bill is passed in the Parliament and gets the assent of the President. The following write up is just an attempt to create a general awareness among the students in respect of the budget proposals and is in no way related to the syllabus.

BUDGET 2005-06

BUDGET 2005-06 – DIRECT AND INDIRECT TAX PROPOSALS – AN OVERVIEW

Budget 2005-06 is a step towards major overhaul of the direct taxes, with increase in basic exemption limit and alteration of tax brackets and reduction in corporate tax to bring them in line with the highest marginal personal income-tax rate.

The budget proposals relating to personal taxation, fringe benefits tax, banking cash transaction tax and corporate taxation are dealt with in the ensuing paragraphs.

Let us first examine the budget proposals relating to personal taxation and their impact on different categories of persons – salaried individuals in different income groups, women assessees and senior citizens.

I PERSONAL TAXATION

The budget, *prima facie,* seems attractive from the personal taxpayer point of view. The increase in the basic exemption limit from Rs.50,000 to Rs.1 lakh across the board coupled with the reduction in tax rates are bound to benefit the middle income group. Introduction of deduction under section 80C in lieu of rebate under section 88 is definitely beneficial to all and to a greater extent to the higher income group, who were denied of this benefit earlier.

First let us look at the budget proposals relating to personal taxation –

1. The Budget proposes to raise the basic exemption limit from Rs.50,000 to Rs.1,00,000 and alter the existing tax brackets. Let us have a look at the existing and revised tax brackets -

Existing tax slabs and rates		**Proposed new tax slabs and rates**	
Upto Rs.50,000	Nil	Upto Rs.1,00,000	Nil
Rs.50,000 – Rs.60,000	10%	Rs.1,00,000 – Rs.1,50,000	10%
Rs.60,000 – Rs. 1,50,000	20%	Rs.1,50,000 – Rs. 2,50,000	20%
Above Rs.1,50,000	30%	Above Rs.2,50,000	30%

   Further, the level at which the surcharge of 10% will apply is to be raised from total income of Rs.8,50,000 to Rs.10,00,000.

2. The threshold exemption level for women has been fixed at Rs.1,25,000 and senior citizens at Rs.1,50,000. However, the same are in lieu of existing rebate under sections 88C and 88B respectively.

Therefore, the existing and revised slab rates for women assessees and senior citizens are:

For Women Assessees

Existing tax slabs and rates		Proposed new tax slabs and rates	
Upto Rs.50,000	Nil	Upto Rs.1,25,000	Nil
Rs.50,000 – Rs.60,000	10%	Rs.1,25,000 – Rs.1,50,000	10%
Rs.60,000 – Rs. 1,50,000	20%	Rs.1,50,000 – Rs. 2,50,000	20%
Above Rs.1,50,000	30%	Above Rs.2,50,000	30%

For Senior Citizens

Existing tax slabs and rates		Proposed new tax slabs and rates	
Upto Rs.50,000	Nil	Upto Rs.1,50,000	Nil
Rs.50,000 – Rs.60,000	10%	Rs.1,50,000 – Rs. 2,50,000	20%
Rs.60,000 – Rs. 1,50,000	20%	Above Rs.2,50,000	30%
Above Rs.1,50,000	30%		

3. Standard deduction for salaried assessees is proposed to be removed in conformity with the growing international practice.

4. A consolidated limit of Rs.1 lakh is proposed to be allowed for tax savings, which will be deducted from the Gross Total Income before calculation of tax. New section 80C is proposed to be introduced. This is in lieu of the existing rebate under section 88. The qualifying amount of Rs.1 lakh is in respect of deductions under section 80C along with sections 80CCC (in respect of contribution to approved pension fund) and 80CCD (contribution to pension scheme of Central Government).

5. In addition to the above consolidated limit of Rs.1 lakh, the following six deductions are to continue to receive the same tax treatment as prevailing –

   (i) Interest paid on housing loan for self occupied property – under section 24

   (ii) Medical insurance premia – under section 80D

   (iii) Specified expenditure on disabled dependent – under section 80DD

   (iv) Expenses for medical treatment of self or dependent member of a HUF – under section 80DDB

   (v) Deduction in respect of interest on loans for pursuing higher studies – under section 80E (However, it is to be noted that the budget proposes to remove the exemption in respect of principal repayment of such loans).

   (vi) Deduction to a person with disability –under section 80U.

6. Section 80L, providing for deduction in respect of interest on savings, deposits etc. is proposed to be omitted.

7. Continuation of tax exemption in respect of interest earned on Non-resident external Account.

   Now, we shall proceed to analyse the impact of the proposed amendments to different persons in different situations – whether the budget has put more money in their pockets or resulted in additional tax burden.

   Situation 1 – Mr. Akash is working in Xansa Ltd. and his gross salary is Rs.1,50,000. He does not have any other income. He does not make any investments.

Particulars	Existing position	Budget proposal
Gross Salary	1,50,000	1,50,000
Less: Standard deduction u/s 16(i)	30,000	Nil
Net Salary/Gross Total Income	**1,20,000**	**1,50,000**
Tax liability	13,000	5,000
Add: Education cess @ 2%	260	100
Total tax liability	**13,260**	**5,100**

Tax savings = 13,260 – 5,100 = Rs.8,160

% of tax savings = 61.54%

Situation 2 – Mrs. Asha is working in Rajdhani Ltd., and her gross salary is Rs.1,50,000. She does not have any other income. She does not make any investments.

Particulars	Existing position	Budget proposal
Gross Salary	1,50,000	1,50,000
Less: Standard deduction u/s 16(i)	30,000	Nil
Net Salary/Gross Total Income	**1,20,000**	**1,50,000**
Tax liability	13,000	2,500
Less: Rebate under section 88C	5,000	Nil
	8,000	**2,500**
Add: Education cess @ 2%	160	50
Total tax liability	**8,160**	**2,550**

Tax savings = Rs.8,160 – Rs.2,550 = Rs.5,610

% of tax savings = 68.75%

Situation 3 – Mr. Giridhar, aged 67 years, receives pension of Rs.15,000 per month. He does not have any other income. He does not make any investments.

Particulars	Existing position	Budget proposal
Gross Salary	1,80,000	1,80,000
Less: Standard deduction u/s 16(i)	30,000	Nil
Net Salary/Gross Total Income	**1,50,000**	**1,80,000**
Tax liability	19,000	6,000
Less: Rebate under section 88B	19,000	Nil
	Nil	**6,000**
Add: Education cess @ 2%	Nil	120
Total tax liability	**Nil**	**6,120**
Additional tax burden = Rs.6,120		

In all the situations above, we have considered salaried assessees whose gross salary is below Rs.2 lakhs. These assessees do not have any other source of income and they do not make any investments. For a salaried individual who does not make any investments, it can be seen that the budget has definitely put more money in their pockets. However, in the case of a senior citizen, the budget has cast additional tax burden since the increase in the basic exemption limit to Rs.1,50,000 does not compensate the benefit derived by him by way of standard deduction and rebate under section 88B.

Now, let us proceed to examine the impact of the budget on a salaried individual in the middle and higher income group. Such individuals generally have money at their disposal and are quite capable of saving Rs.1 lakh and depositing money in banks, interest from which was so far available as deduction under section 80L.

Situation 4 – Mr. Karan is working with Hindustan Lever Ltd. as sales officer. His gross salary is Rs.3,50,000 p.a. He deposits Rs.60,000 in PPF, Rs.30,000 in ICICI infrastructure bonds and pays life insurance premium of Rs.10,000. His interest income from bank deposits etc. is Rs.13,000 and from government securities is Rs.5,000.

Particulars	Existing position	Budget proposal
Gross Salary	3,50,000	3,50,000
Less: Standard deduction u/s 16(i)	30,000	Nil
Net Salary	**3,20,000**	**3,50,000**

Income from other sources	18,000	18,000
Gross Total Income	**3,38,000**	**3,68,000**
Less: Deduction under Chapter VI-A		
Under section 80C	Nil	1,00,000
Under section 80L	15,000	Nil
Total Income	**3,23,000**	**2,68,000**
Tax liability	70,900	30,400
Less: Rebate under section 88 (15% of Rs.1,00,000)	15,000	Nil
	55,900	**30,400**
Add: Education cess @ 2%	1,118	608
Total tax liability	**57,018**	**31,008**

Tax Savings = Rs.57,018 – Rs.31,008 = Rs.26,010

% of tax savings = 45.62%

Situation 5 – Mr. Anirudh is working with Times Ltd. as a General Manager. His gross salary is Rs.9,00,000 p.a. He deposits Rs.60,000 in PPF, Rs.50,000 in ICICI infrastructure bonds and pays life insurance premium of Rs.12,000. His interest income from bank deposits etc. is Rs.23,000 and from government securities is Rs.5,000.

Particulars	Existing position	Budget proposal
Gross Salary	9,00,000	9,00,000
Less: Standard deduction u/s 16(i)	20,000	Nil
Net Salary	**8,80,000**	**9,00,000**
Income from other sources	28,000	28,000
Gross Total Income	**9,08,000**	**9,28,000**
Less: Deduction under Chapter VI-A		
Under section 80C	Nil	1,00,000
Under section 80L	15,000	Nil
Total Income	**8,93,000**	**8,28,000**

Tax liability	2,41,900	1,98,400
Less: Rebate under section 88 (not available since gross total income is higher than Rs.5,00,000)	Nil	Nil
	2,41,900	**1,98,400**
Add: Surcharge @ 10% (since total income exceeds Rs.8,50,000)	24,190	Nil
	2,66,090	**1,98,400**
Add: Education cess @ 2%	5,322	3,968
Total tax liability	**2,71,412**	**2,02,368**

Tax Savings = Rs.2,71,412 – Rs.2,02,368=Rs.69,044

% of tax savings = 25.44%

Thus, it is not only the middle income class but also the higher income class who will reap the advantage of tax savings from this budget.

Thus, the positive features of the budget proposals on personal taxation are –

1. The proposed replacement of rebate for savings in specified schemes under section 88 by a deduction under section 80C from gross total income will have the impact of tax savings to the tune of the product of the tax rate applicable to a person(depending on the tax bracket he falls in) and his investments (i.e. a person who has a gross total income of Rs.4 lakhs is in the 30% tax bracket and if he invests 1 lakh in specified schemes, he would save Rs.30,000, being 30% of Rs.1 lakh). Earlier, the tax rebate was at the rate of 15% for persons whose gross total income exceeded Rs.1,50,000 and nil for those persons whose gross total income exceeded Rs.5,00,000. Therefore, this amendment would very much find favour of the middle and higher income earners.
2. Further, the sub-limits under section 88 in respect of repayment of housing loan (Rs.20,000), payment of tuition fees (Rs.12,000 per child per annum) and PPF, LIC etc. (Rs.70,000) under the existing tax regime are now proposed to be removed. So, if a person is making a repayment of upto Rs.1,00,000 towards principal portion of housing loan, he would be eligible for a rebate for the full amount and need not make any further investments. This would be in addition to deduction for interest on housing loan under section 24. This is a welcome proposal.
3. The applicability of surcharge for total income of over Rs.10 lakhs as against the existing Rs.8.5 lakhs would be a great relief for persons in the tax bracket of Rs.8.5 lakhs to Rs.10 lakhs.

4. Continuation of exemption on interest on NRE A/c will benefit non-residents. This exemption was earlier proposed to be removed by the Finance (No.2) Act, 2004 w.e.f. A.Y.2006-07.

However, the following difficulties and genuine hardship may be noted –

1. By removing standard deduction on salary, the gross income of the salaried would be subject to tax. This is against the principle of income-tax law and would put the salaried class in a disadvantageous position as compared to their business/professional counterparts, who would continue to be entitled to set-off their expenditure against their income. Whereas the revision in the basic exemption limit and tax slabs would be uniformly applicable to both the salaried and businessmen, the removal of standard deduction would affect only the salaried class.
2. The proposed removal of deduction under section 80L might affect inflow of deposits into banks etc.
3. The deduction under section 80E is proposed to be restricted to only repayment of interest on loans taken for higher education. Upto now, the deduction was available both in respect of principal and interest repayments. This will result in genuine hardship to poor students.
4. As can be seen from the illustration in situation 3 above, the senior citizens in receipt of pension would be at the losing end due to removal of rebate under section 88B and standard deduction. The increase in their basic exemption limit to Rs.1,50,000 would not compensate this loss. Further, to a senior citizen who has invested his retirement benefits in monthly income schemes of post office/banks to derive regular monthly income in addition to pension, the budget would result in imposition of additional tax burden due to removal of deduction under section 80L.

II FRINGE BENEFITS TAX

Budget 2005-06 proposes to impose a new tax by the name of “Fringe Benefits Tax” on certain expenses incurred by the employers. These expenses are deemed to be in the nature of fringe benefits extended to employees. The Finance Minister, in his speech, had specified that this tax would be on those benefits which are usually enjoyed collectively by the employees. This tax is to be borne by the employer. However, transport services for workers and staff and canteen services in an office or factory will be outside the tax net. Further, this tax would not be leviable on those perquisites which are taxable in the hands of the employee under Chapter IV of the Income-tax Act, 1961.

Fringe benefits would mean –

(a) any privilege, service, facility or amenity, directly or indirectly, provided by an employer to his employees (including former employee or employees) by reason of their employment.

(b) Any reimbursement, directly or indirectly, made by the employer to his employees for any purpose;

(c) Any free or concessional ticket provided by the employer for private journeys of the employees and their family members; and

(d) Any contribution by the employer to an approved superannuation fund.

The fringe benefits would be deemed to have been provided if the employer has, in the course of his business or profession, incurred any expense on or made any payment for the following purposes mentioned in column (2) of the table below. The percentage of expenditure to be taken into account for computing the value of the benefit is given in column (3) of the table below. The rate of tax is 30% on the value of fringe benefits computed by applying the percentages specified in column (3) to the specified expenditure incurred as indicated in column (2) of the table below.

(A)	Entertainment	50%
(B)	Festival celebrations	50%
(C)	Gifts	50%
(D)	Use of club facilities	50%
(E)	Provision of hospitality of every kind by the employer to any person	50%
(F)	Maintenance of any accommodation in the nature of guest house	50%
(G)	Conference	50%
(H)	Employee welfare	50%
(I)	Use of health club, sports and similar facilities	50%
(J)	Sales promotion including publicity	50%
(K)	Conveyance, tour and travel including foreign travel	20%
(L)	Hotel, boarding and lodging	20%
(M)	Repair, running and maintenance of motorcars.	20%
(N)	Repair, running and maintenance of aircrafts	20%
(O)	Consumption of fuel other than industrial fuel	20%
(P)	Use of telephone	10%
(Q)	Scholarship to the children of the employees	100%

However, in the case of an employer, engaged in the business of hotel, the value of fringe benefit in respect of provision of hospitality referred to in (E) above would be only 5% of the expenditure. Further, in the case of an employer engaged in the business of carriage of passengers or goods by motor car, the value of fringe benefit in respect of repairs, running and maintenance of motor car and consumption of fuel other than industrial fuel would be only 5% of the expenditure. Similarly, in the case of an employer engaged in the business of carriage of passengers or goods by aircraft, the value of fringe benefit in respect of repairs, running and maintenance of aircraft and consumption of fuel other than industrial fuel would be only 5% of the expenditure

The impact of introduction of fringe benefit tax is as under –

1. Firstly, it can be viewed that the fringe benefit tax is not an income tax but is in the nature of an expenditure tax, since the tax base consists of the cost of fringe benefits to the employees. Further, the cost of the fringe benefits constituting the tax base requires to be deemed as income. Similar provisions exist in section 115JB.
2. This tax is to be uniformly levied on all employer-assessees, whether they are individuals, firms or companies. The tax would be levied even if the entity is a loss making one. Further, it would also be applicable to those assessees who are otherwise exempt from income-tax like export-oriented industries, industries in free trade zones/special economic zones etc.
3. Further, the employer would have to file a separate return of fringe benefits over and above the normal income-tax return. That apart, separate provisions for assessment, issue of notice, payment of tax and advance tax have been prescribed, which would increase the paper work and the administrative burden of the tax department.

III BANKING CASH TRANSACTION TAX

The Budget proposes to impose a new tax called "Banking Cash Transaction Tax" as an anti tax-evasion measure on all withdrawals of cash of over Rs.10,000 on a single day at the rate of 0.1%. The reason for levy of this tax seems to be that the payment of tax would leave an audit trail and in the process help to unearth black money and assets. This tax is also proposed to be levied on –

(i) a person who purchases a bank draft or a banker's cheque or any other financial instrument on payment of cash exceeding Rs.10,000 on a single day from any scheduled bank.

(ii) a person who encashes his term deposit, whether on maturity or otherwise, with a scheduled bank and receives cash exceeding Rs.10,000 on a single day from such bank on such encashment

However, this tax would not be levied where the amount of term deposit is credited to any account with the bank.

The levy of this tax might affect business operations since cash withdrawal is required for business purposes like payment of wages to workmen etc. The levy of such a tax would also be harsh on the agricultural sector, which has to provide cash to the farmers who are still in the unorganized sector and need cash to part with their produce.

It is significant to note that Rule 6DD(j) of the Income-tax Rules, 1962 provides for various situations where cash payment can be made which will not be hit by the provisions of section 43B. Thus, the Income-tax Act, 1961, itself has recognized the situations where cash withdrawals beyond Rs.20,000 would be necessary to carry on business and other activities.

Further, the banking cash transaction tax would increase the cost to the business which would lead to further inflation.

IV CORPORATE TAXATION

The corporate tax reform is proposed to be implemented through reduction in corporate tax rate to align with the highest marginal personal income tax rate and reduction in depreciation rate to bring them in tune with the rate that would enable the investor to replace the asset before the end of its economical life.

The major budget proposals relating to corporate taxation are –

1. Reduction of corporate tax rate from 35% to 30% and increase in surcharge from 2.5% to 10% to align them with the highest marginal personal income tax rate.
2. Reduction in rate of general plant and machinery from 25% to 15%.
3. Initial depreciation rate to be increased from 15% to 20%.
4. The requirement of 10% increase in installed capacity for availing of the benefit of initial depreciation to be removed.

Let us now examine the impact of these proposals on a corporate with the help of a small illustration.

The following are the particulars relating to X Ltd. for the financial year.

Particulars	**Rs.**
Profit before depreciation on plant and machinery	65,00,000
Particulars of Fixed Assets -	
Plant and machinery (WDV at the beginning of the year)	55,00,000
New plant and machinery purchased during the year and put to use for 9 months. There has been an increase in installed capacity by more than 10%.	10,00,000
X Ltd. incurs Rs.8 lakhs on fringe benefits towards employees during the year, the particulars of which are as follows -	
Expenses on entertainment	2,00,000
Festival expenses	1,00,000
Use of club facilities by employees	3,00,000
Use of telephone by employees	50,000
Employee welfare	50,000
Hotel, boarding and lodging	1,00,000

Further, X Ltd. has also withdrawn cash to the tune of Rs.18 lakhs out of which Rs.15 lakhs represent the aggregate of those cash withdrawals which exceeded Rs.10,000 per day.

Examine the effect of the budget proposal on the tax liability of X Ltd.

Computation of tax liability of X Ltd.

Particulars	**Existing position**	**Particulars**		**Budget proposal**
Profit before depreciation on plant and machinery	65,00,000	Profit before depreciation on plant and machinery		65,00,000
Less: Depreciation on plant and machinery		Depreciation on plant and machinery		
@25% of 65 lakhs	16,25,000	On opening WDV of Rs.55 lakhs @15%	8,25,000	
@15% of 10 lakhs	1,50,000	On new machinery of Rs.10 lakhs @ 35%	3,50,000	11,75,000
Profit after depreciation	**47,25,000**	**Profit after depreciation**		**53,25,000**
Tax @35%	16,53,750	Tax @30%		15,97,500
Add: Surcharge @ 2.5%	41,344	*Add:* Surcharge@10%		1,59,750
	16, 95,094			**17,57,250**
Add: Fringe benefits tax	Nil	*Add:* Fringe benefits tax		1,05,000
		30% of Rs.3,50,000		
		(See working note below)		
Add: Banking cash transaction tax	Nil	*Add:* Banking cash transaction tax (0.1% of Rs.15 lakhs)		1,500
Total tax liability	**16, 95,094**	**Total tax liability**		**18,63,750**

Thus, we can see that the tax liability of X Ltd. would go up by Rs.1,68,656 as a result of the budget proposals. Therefore, even though the corporate tax rate has been reduced to 30%, the impact of increase in surcharge, reduction in rate of depreciation on general plant and machinery, imposition of fringe benefits tax and banking cash transaction tax might result in increase their overall tax liability. However, the actual impact on the corporates would vary, depending on their investment in plant and machinery and the amount incurred by them by way of fringe benefits.

Working note on computation of value of fringe benefits -

Particulars	Expenditure	% to be taken for computing value of fringe benefit	Value of fringe benefit
Expenses on entertainment	2,00,000	50%	1,00,000
Festival expenses	1,00,000	50%	50,000
Use of club facilities by employees	3,00,000	50%	1,50,000
Use of telephone by employees	50,000	10%	5,000
Employee welfare	50,000	50%	25,000
Hotel, boarding and lodging	1,00,000	20%	20,000
Total value of fringe benefit			**3,50,000**

The other budget proposals relating to corporate taxation are –

1. Credit to be allowed for Minimum Alternate Tax (MAT) paid under section 115JB.
2. Withholding tax on technical services to be reduced from 20% to 10%.
3. Terminal dates for exemption to be extended from 31st March 2005 to 31st March 2007 in the following cases –
   (i) Weighted deduction of 150 per cent of expenditure on in-house research and development facilities of companies engaged in biotechnology, pharmaceuticals, electronics, telecommunication, chemicals or any other notified product;
   (ii) Deduction of profits of new industrial undertakings in Jammu and Kashmir;
   (iii) 100% deduction of profits of companies carrying on scientific research and development and approved by the Department of Scientific and Industrial Research.
4. Terminal date for exemption from tax on agreements to acquire aircraft or aircraft engines on lease to be extended to 30th September, 2005.

SIGNIFICANT INDIRECT TAXES PROPOSALS – AN OVERVIEW

The Finance Bill, 2005 has made the following proposals in respect of Central Excise & Customs:

1. Section 5A of the Central Excise Act, 1944 has been proposed to be amended to provide that manufacturer has to compulsorily avail the benefit of the exemption notification when the exemption is available unconditionally.

   Therefore, now the manufacturers would not be able to avail credit and pay duty by utilizing it. They will have to compulsorily opt for the exemption route.

2. Section 28H of the Customs Act is proposed to be amended to include one more matter in the list of matters on which an advance ruling can be sought. It is proposed that now the advance ruling can be obtained in respect of determination of rules of origin of goods and such other matters relating thereto.

   The proposal of the bill expands the scope of the matters on which advance ruling can be obtained.

3. The Finance Bill seeks to amend section 23A of the Central Excise Act, 1944 and section 28E of the Customs Act, 1962. The bill proposes to include a (i) joint venture in India as an "applicant" and (ii) to empower the central Government to notify any class or category of persons as an "applicant",

   The intention of the legislation it seems is to expand the base of the applicants for advance ruling. Now more people can be benefited by obtaining advance ruling.

4. It is proposed to empower the settlement commission to send back the case to the Tribunal if the assessee has not cooperated.

   Under the current provisions, the persons who have filed appeals to the Appellate Tribunal before 29.2.2000 can withdraw their case from the Tribunal and approach the settlement commission. The Bill seeks to empower the commission to send back such a case back to the Tribunal in case the assessee does not cooperate. However, the word "cooperated" has not been defined in the provision.

5. Sections 35B & 35E Central Excise Act & sections 129A & 129D of Customs Act are proposed to be amended. A Committee of two Chief Commissioners shall be constituted which will review the orders passed by the Commissioner of Central Excise/Customs and Commissioner of Central Excise/Customs (Appeals).

   Under the current provisions the orders of the Commissioner of Central Excise/Customs & Commissioner of Central Excise/Customs (Appeals) are reviewed by members of CBEC & Commissioner of Central Excise/Custom respectively. If the reviewing authority finds that the orders are not proper, it can direct the commissioner of Central Excise/Customs or any officer to file the appeal against the said order.

   The Finance Bill proposes that these orders shall now be reviewed by a Committee of Chief Commissioners. It is hoped that such an amendment will improve the quality of the review of the orders substantially and ultimately may result in reduction in the pendency of huge cases before CESTAT.

6. The limit of turnover for claiming the benefit of SSI exemption has been increased from Rs.300 lakhs to Rs.400 lakhs. However, Notification No.9/2003 has been rescinded.

   Now, therefore, the number of units benefiting from SSI concession will increase but on the same time they will loose the option of availing credit and paying 60% of the normal duty.

7. Clause 87 of the bills seeks to insert a chapter note in chapter 15 of the first schedule to the Central Excise tariff Act, 1985 with retrospective effect from 1.3.1986 so as to provide that in respect of refined edible oils the process of refining shall amount to manufacture.

   In case of "*Shyam Oil Cake Ltd. V. CCEx., Jaipur, 2004 (174) E.L.T. 145",* the Supreme Court had held that neither the Section note nor the Chapter note nor the Tariff item gave any indication that the refining process would amount to manufacture. As actual manufacture had not taken place, deeming provisions could not be invoked in the absence of specific statement that the process would amount to manufacture.

   This proposal seems to remove the lacunae pointed by the Apex Court. The proposal adds a chapter note mentioning that process of refining shall amount to manufacture.

The following are the major proposals about changes in duty structure in Excise and Customs:

EXCISE

Changes come into effect immediately unless otherwise specified.

1. Surcharge on pan masala and tobacco products

An additional excise duty, by way of surcharge, is being levied on pan masala and certain specified tobacco products to finance, the National Rural Health Mission. This additional duty will be charged at prescribed specific rates on cigarettes, and at a rate equal to 10% of the aggregate of normal rates of excise duties payable on pan masala and other tobacco products. This surcharge has not been levied on biris.

2. Imposition and increase in duty

(1) Imposition

   (a) Excise duty of 8% with CENVAT credit has been imposed on mosiac tiles. SSI exemption is available.

   (b) Excise duty of 16% has been imposed on road tractors (of engine capacity more than 1800 cc) for road trailers.

   (c) Excise duty of 2% has been imposed on branded articles of jewellery. The process of affixing or embossing the brand or trade name on the article of jewellery shall amount to 'manufacture'.

(2) Excise duty has been raised on iron and steel of chapter 72 from 12% to 16%.

(3) Excise duty on molasses has been increased from Rs.500 per metric tonne to Rs.1000 per metric tonne.

3. Relief measures

(1) Excise duty has been reduced from 24% to 16% on air conditioners.

(2) Excise duty has been reduced from 24% to 16% on tyres, tubes and flaps.

(3) Excise duty has been reduced from 16% to 12% (with Cenvat credit) on matches made by mechanized and semi mechanized sectors.

(4) Excise duty on imitation jewellery has been reduced from 16% to 8%.

(5) Excise duty has been reduced from 16% to 8% on cakes and pastries.

4. Agriculture and food processing

(1) Excise duty of Re. 1 per kg. on refined edible oils and Rs.1.25 per kg. on vanaspati, bakery shortening and inter-esterfied, re-esterified, elaidinised fats, has been exempted.

(2) Tea and tea waste have been exempted from additional duty of excise of Re. 1 per kg.

5. Textiles

(1) Excise duty on polyester filament yarn (PFY), including polyester textured yarns has been reduced from 24% to 16%

(2) Optional duty has been prescribed for processed filament yarns (including polyester filament yarn) manufactured from yarn procured from outside by independent processors. Such yarn would either attract Nil excise duty without availment of Cenvat credit or pay 8% excise duty with Cenvat credit.

6. Petroleum

(1) Basic excise duty rates on certain petroleum products have been revised as under:

Sl.no.	**Particulars**	From	To
(a)	Petrol	23%	8% +Rs.5.00/litre
(b)	Diesel	8%	8% +Rs.1.25/litre
(c)	Kerosene for public distribution	12%	Nil
(d)	LPG for domestic use	8%	Nil
(e)	Light Diesel Oil	16% +Rs.1.50/litre	16% + Rs.2.50/litre

(2) Additional duty of excise on motor spirit and high-speed diesel oil has been increased from Re.1.50 per litre to Rs.2 per litre. This amount goes to Central Road Fund.

(3) There is no change in special additional excise duty of Rs.6.00 per litre on motor spirit.

7. National calamity contingent duty (NCCD)

For replenishment of the National Calamity Contingent Fund, duty on following items was imposed by the Finance Act, 2003

(1) 1% on polyester filament yarn, motorcars, multiutility vehicles, and two-wheelers;

(2) Rs.50 per metric tonne on domestic crude oil.

This levy was valid for one year (up to 29.2.2004) and subsequently was extended up to 31.3.2005. It is proposed to extend this levy without any time limit.

8. Retail sale price (RSP) based assessment

Abatement from retail price for levy of excise duty on air conditioners has been reduced from 35% to 30%, consequent to reduction in excise duty from 24% to 16%.

CUSTOMS

Changes come into effect immediately unless otherwise specified.

1. Additional duty of customs

An additional duty of customs of 4% shall be levied on all items imported into India. This levy will be to partly compensate for the internal taxes like sales tax, proposed State VAT, central sales tax, which apply to sale, purchase or transportation of goods in India. Initially, this additional duty will be charged only on Information Technology Agreement (ITA) bound items and on specified inputs/raw materials for manufacture of electronics/information technology items, which have been exempted from customs duty. This duty will not be charged on information technology software. This additional duty will not be included in the assessable value for levy of education cess on imported goods. Manufacturers will be able to take credit of this additional duty for payment of excise duty on their finished products.

2. Peak rate of ad valorem customs duty reduced

(1) Peak rate of customs duty on non-agricultural products has been reduced from 20% to 15% with a few exceptions.

(2) Ad valorem component of customs duty on textile fabrics and garments has been reduced from 20% to 15%. There has, however, been no change in specific component of customs duty.

3. Metals and their inputs

(1) Customs duty has been reduced from 15% to 10% on primary and semi-finished forms of stainless steel, other alloy steel and ferro-alloys, aluminium, copper, zinc, tin etc.

(2) Customs duty on lead has been reduced from 15% to 5%, on articles of lead from 20% to 10% and on battery separators from 20% to 5% .

4. Agriculture & food processing

(1) Customs duty on cut flowers including orchids has been increased from 30% to 60%.

(2) Customs duty on cloves has been reduced from 70% to 35%.

(3) Customs duty on refrigerated goods transport vehicles has been reduced from 20% to 10%.

5. Research and development

(1) Customs duty on 9 specified equipment for biotech and pharmaceutical sectors has been reduced from 20% to 5%.

(2) Customs duty exemption presently available to capital goods and raw materials to a company for any Research and Development (R&D) project funded by Government or CSIR has been extended to R&D projects funded by CSIR, ICMR, ICAR, UGC, DRDO and AICTE also.

6. Information technology

(1) Customs duty has been exempted on specified items covered under the Information Technology Agreement (ITA). With this, all 217 ITA bound items are now fully exempt from customs duty.

(2) All goods imported for the manufacture of ITA bound items have been exempted from customs duty subject to end-use condition.

(3) Customs duty has been exempted on specified electronic components.

(4) Customs duty exemption presently available to specified capital goods for Information Technology/Electronics sector has been extended to some more capital goods.

(5) Customs duty has been reduced from 20% to 10% on optical fibres/bundles and optical fibre cables of heading 9001.

(6) Customs duty exemption presently available to specified telecom network equipment and parts thereof upto 31.3.2005, when imported by telecom service providers, has been continued without any time limit.

7. Petroleum products

(1) Customs duty on crude petroleum and petroleum products has been reduced as follows:

- (a) Crude petroleum from 10% to 5%;
- (b) Kerosene for public distribution system from 5% to Nil;
- (c) LPG for domestic use from 5% to Nil;
- (d) Motor Spirit (Petrol) from 15% to 10%;
- (e) High Speed Diesel oil from 15% to 10%; and
- (f) Other petroleum products from 20% to 10%.

(2) Additional duty of customs on motor spirit and high speed diesel oil has been increased from Re.1.50 per litre to Rs. 2 per litre.

8. Chemicals and petrochemicals

(1) Customs duty on industrial (denatured) ethyl alcohol has been reduced from 15% to 10%.

(2) Customs duty on molasses has been reduced from 15% to 10%.

9. Capital goods

(1) Customs duty on specified machinery/equipment for use in Inland Container Depot (ICD)/Container Freight Station (CFS) has been reduced from 20% to 10%

(2) Customs duty on railway locomotives, railway rolling stock and railway equipment and their parts (of chapter 86) has been reduced from 20% to 10%.

(3) Concessional rate of customs duty of 5% presently available to specified goods designed for use in leather/footwear industry has been extended to 7 more specified machinery.

(4) Customs duty on specified parts of printing presses has been reduced from 20% to 10%.

(5) Customs duty on specified textile machinery, and raw materials and parts for manufacture of such machinery, has been reduced from 20% to 10%.

(6) Customs duty exemption for specified inputs for manufacture of leather goods, travel goods, footwear, etc. for export has been extended to some more items, subject to the existing 3% overall value limit.

10. National calamity contingent duty (NCCD)

For replenishment of the National Calamity Contingent Fund, duty of Rs. 50 per metric tonne on imported crude oil, and a duty of 1 % on polyester filament yarn, motor cars, multiutility vehicles, and two-wheelers was imposed in Finance Act, 2003. This levy was valid for one year (up to 29.2.2004) and subsequently extended up to 31.3.2005. It is proposed to extend this levy without any time limit.

11. Baggage

Customs duty on passenger baggage has been reduced from 40% to 35%.

12. Miscellaneous

(1) Customs duty on second hand motor cars/motor cycles has been reduced from 105% to 100%.

(2) Customs duty on Atmospheric Water Generators has been reduced from 20% to 5%.

(3) Customs duty on specified parts of battery operated road vehicles has been reduced from 20% to 10%.

SERVICE TAX

Major proposals in the field of service tax are:

1. An exemption scheme for small service providers has been prescribed. Service providers, whose aggregate value of taxable services provided during the preceding financial year does not exceed Rs. 4 lakhs will be exempted from service tax upto an aggregate value of taxable services of Rs. 4 lakhs in a financial year. The proposed exemption scheme would be applicable from 1.04.2005.

2. Exemption has been provided from service tax on business auxiliary service, to person producing/processing goods, from the inputs received from a manufacturer and sending the resultant product to the same manufacturer for further manufacture of final products, which are cleared on payment of excise duty. The above change will come into effect immediately.

3. Following new services are being proposed to be covered under the service tax law:

   (1) Transport of goods through pipeline or other conduit;

   (2) Site preparation and clearance, excavation, earth moving and demolition services, other than those provided to agriculture, irrigation and watershed development;

   (3) Dredging services of rivers, ports, harbours, backwaters and estuaries;

   (4) Survey and map making other than by Government Departments;

   (5) Cleaning services other than in relation to agriculture, horticulture, animal husbandry or dairying;

   (6) Membership of clubs or associations;

   (7) Packaging services;

   (8) Mailing list compilation and mailing; and

   (9) Construction of residential complexes having more than twelve residential houses or apartments together with common areas and other appurtenances.

   The above changes will come into effect from a date to be notified after the enactment of the Finance Bill, 2005.

4. It has been proposed to increase the scope of certain existing services viz., commercial or industrial construction service, erection, commissioning or installation service, maintenance or repair service, broadcasting service etc.

   The above changes will come into effect from a date to be notified after the enactment of the Finance Bill, 2005.

5. The Finance Act, 1994 is being amended to:

   (a) extend the scope of 'taxable services' so as to include the 'services to be provided' and to clarify that taxable services would include such services provided from outside India to a recipient in India [Section65(105)];

   (b) clarify that payments received, before, during, or after the provision of taxable service, would form part of gross amount for charging service tax (Section 67);

   (c) incorporate enabling provisions for registration and filing of return by persons or class of persons other than person liable to pay service tax (Section 69 and 70);

   (d) extend the powers to issue show cause notice and determine the amount of short levy to a Central Excise Officer (Sections 73). Consequential changes have also been made in sections 74, 78, 84, 85 and 86;

(e) make provisions regarding powers of adjudication and adjudication procedures of service tax cases;

(f) allow an existing Joint Venture in India to avail the benefit of Advance Ruling. The Central Government is also being empowered to notify any class or category of persons as eligible for availing of the benefit of Advance Ruling (Section 96A).

The change specified in 1(a) above will come into effect from a date to be notified after the enactment of the Finance Act, 2005. The other changes mentioned above will come into effect on the date of enactment of Finance Act, 2005.

6. The Service Tax Rules are being amended so as to:

(a) prescribe that the invoice is to be issued within 14 days from date of completion of provision of service or receipt of payment, whichever is earlier [Rule 4A(1)];

(b) prescribe that due date for service tax payment by all service tax assessees would be 5th of the following month or quarter, as the case may be (Rule 6);

(c) enable centralized registration of more than one premises (Rule 4);

(d) prescribe that liability of payment of service tax on business auxiliary services provided by the distributors of mutual funds will be on the recipient of service, namely, mutual funds (Rule 2).

The above changes will be effective for services rendered on or after 1" April, 2005.

This booklet gives an overview on the taxation proposals in the budget. We have given the likely impact of the major budget proposals in our discussion above. However, it is possible to have different views on each proposal.

HIGHLIGHTS – ECONOMIC SURVEY 2004-2005

- Economy poised to achieve 6.9 per cent growth in 2004-05.
- Inflation down to 5 per cent.
- Growth upswing despite hardening in global oil/steel prices/tsunami.
- Agriculture and allied sector looking up despite deficient rainfall.
- Shortfall in Khariff to be offset by good Rabi crop.
- Buffer stock position comfortable/decline in food grains may not affect.
- Non-food grain agriculture to grow by over 1 per cent.
- Share of agriculture in GDP down by 3.5 per cent since 2001-02.
- Industrial production to be up by 8.4 per cent in 2004-05.
- Electricity generation to rise by 6.5 per cent.
- Exports to increase by 23.1 per cent/imports by 32.1 per cent.
- Services sector records 8.9 per cent growth.
- Foreign Exchange Reserves to cross 130 billion dollars.
- Exports to double to 150 billion dollars in 2008-09.
- 30 per cent increase in agriculture credit, flow to double in 3 years.
- Significant decline in non performing assets of Banks.
- Marginal increase in deposit rates/interest on housing loans firm up.
- Revenue deficit sought to be lowered to 2.5 per cent of GDP.
- Budget estimates in Central finances to improve in the last quarter.
- Consolidated fiscal deficit of Centre/States to fall by 7.9% of GDP.
- IPO grew 5 times to Rs.35859 crore in 2004.
- Significant improvement in savings and investment observed.
- Improvement seen in poverty and employment ratio.
- Major programmes to achieve NCMP targets.

Budget 2005-06

Poverty and Unemployment

- Budget 2005-06 agrees that a significant proportion of our people are poor. And apart from income poverty, other indicators of poverty are illiteracy, disease, infant mortality, malnutrition, absence of skills and unemployment. In order to overcome these problems, the following measures are suggested:

- Assured irrigation facilities to additional 1 crore hectares of land over a period of 5 years. This would generate employment for an additional 1 crore people at the rate of 1 person per hectare.
- Sectors with potential for generating employment will receive the highest attention of the government. These include food processing industry, textile sector, information technology and construction sectors.
- The National Food for Work Programme has been converted into National Rural Employment Guarantee Scheme. With an increased allocation of Rs.11,000 crore, this scheme will provide livelihood security for crores of poor families.
- In order to strengthen the primary health care, the National Rural Health Mission will be launched. More stress will be given to training of health volunteers, providing more medicines and strengthening the primary and community health services.
- The Antyodaya Anaa Yojana which covered 2 crore Below Poverty Line (BPL) families will now cover 2.5 crore families in 2005-06.
- The Integrated Child Development Services (ICDS) looks into overall development of children. The allocation for ICDS has been increased from Rs.1623 crore in 2004-05 to Rs.3142 crore in 2005-06. The allocation to other programmes relating to child welfare like `Sarva Shiksha Abhiyan' and `Mid-day Meal' has also increased.
- Rajiv Gandhi National Drinking Water Mission aims at providing safe drinking water to more and more rural habitations. The outlay for the Mission has been increased so that more areas can be covered.
- In order to empower SC/ST more budget allocations have been made than the previous budget.
- Special concessions have been made for minorities. These include increasing the equity support for the National Minorities Development and Finance Corporation, opening new schools for minority population, giving assistance for recruitment and posting of urdu teachers and providing financial assistance to meritorious candidates from minority communities.
- A Backward Regions Grant Fund has been established. Under this, Bihar, J&K and North Eastern Region will get special assistance.
- In order to provide basic infrastructure to the poor, the Rural Infrastructure Development Fund which was established last year will get a corpus of Rs.8000 in 2005-06.

Bharat Nirman

Bharat Nirman has been conceived as a business plan, to be implemented over a period of 4 years, for building infrastructure, especially in rural areas. It will have six components, namely, irrigation, roads, water supply, housing and rural electrification and rural telecom connectivity. Budget lays down certain targets which are to be achieved by 2009. These are:

- To bring an additional one crore hectares under assured irrigation.

- To connect all villages that have a population of 1000 with a road.
- To construct 60 lakh additional houses for the poor.
- To provide drinking water to the remaining 74,000 uncovered habitations.
- To reach electricity to the remaining 1,25,000 villages and offer electricity connection to 2.3 crore household.
- To give telephone connectivity to the remaining 66,822 villages.

Investment

Budget lays emphasis on enhancing public and private investments in infrastructure required to support expansion, diversification and value-addition in agricultural, industrial and services sectors. An equity support of Rs.14,040 crore and loans of Rs.3,554 crore to central PSEs has been announced. However, the Budget recognizes that the capital markets, banks, insurance companies, pension funds and superannuating funds would have a crucial role in mobilizing and disbursing the financial resources required to sustain high investment.

Agriculture

- Following proposals are made w.r.t. agriculture –
- The Ministry of Agriculture will prepare a roadmap for agricultural diversification. It will focus on fruits, vegetables, flowers, dairy, poultry, fisheries, pulses and oilseeds.
- The National Horticulture Mission will be launched to look into research, production, post-harvest management, processes and marketing of horticulture.
- A progromme for massive re-plantation and rejuvenation of tea will be launched.
- A new scheme called Development/Strengthening of Agricultural Marketing Infrastructure, Grading and Standardization will be launched. The aim is to induce large investments from the private and cooperative sectors for setting up agricultural markets, marketing infrastructure and support services.
- Budget provides additional funds for promoting micro-irrigation in 2005-06.
- Commericla banks, RRBs and cooperative banks would be asked to increase the flow of credit to rural households and farm households by 30 per cent in 2005-06.
- In order to revive cooperative banks in India, a Task Force was constituted. The Task Force has recommended special financial assistance to wipe out accumulated losses, strengthening the capital base of cooperative institutions, institutional restructuring and change in the legal framework to empower RBI to enforce prudent financial management.
- The National Agricultural Insurance Scheme which has been in operation since 1999-2000 will continue in 2005-06.
- Micro Finance Institutions (MFIs) provide small scale credit and other financial services to low income households and small informal businesses Government intends to promote MFIs in a big way. The existing Micro Finance Development Fund has been

redesignated as Micro Finance Development and Equity Fund with an increase corpus of Rs.200 crore.

- A knowledge Centre using modern information and communication technology is proposed to be opened in every village.
- A National Fund for Strategic Agricultural Research has also been created with initial provision of Rs.50 crore.

Manufacturing

- In order to strengthen the operations of the manufacturing sector and sharpen its competitiveness, a new scheme called "Manufacturing Competitiveness Programme" is proposed in the Budget.
- Textile and handloom sectors have got additional benefits and financial help.
- A new financial package has been proposed to revitalize the sugar industry.
- Government intends to provide a stable policy environment and necessary incentives to help pharmaceutical and biotechnology industries to become world leaders.
- The small scale industry which now will be treated as the small and medium enterprises sector will have a further liberalized capital subsidy scheme. A SME growth Fund has been created and knowledge based industries such as pharma, biotech and IT will be provided equity strength through this fund.
- 108 items, including 30 items of textiles products, have been dereserved from the list of items reserved for small scale industries.
- In order to develop skill among youths, 100 ITIs have been identified and linked with industry.
- An ambitious target of U.S. $ 50 billion for exports by the year 2008-09 has been fixed in order to double India's share in world exports to 1.5 per cent.
- FDIs, apart from automobiles, software, tele-communication and electronic sector, will also be welcomed in other sectors such as mining, trade and pension.

Infrastructure

- By the end of January 2005, a tele-density of 8.75 per cent has been achieved and in 5.20 lakh village public telephones (VPTs)have been installed. The Government intends to undertake VPTs in the next three years to the remaining 66,822 villages.
- The outlay for National Highway Development has been increased from Rs.6,514 crore in 2004-05 to Rs.9,320 crore in 2005-06.
- A massive programme for rural electrification will begin in 2005-06 with the objective of covering 1.25 lakh villages in five years.
- The allocation for the rural housing scheme called Indira Awas Yojana has been increased and about 15 lakh houses will be constructed next year.

- A Special Purpose Vehicle (SPV) has been proposed to fund the infrastructural projects which need huge financial support. Roads, airport and tourism would be the sectors which would benefit from SPV. When these projects will be implemented, the foreign exchange resources could be withdrawn for financing necessary imports.

Financial Sector

- The Banking Regulation Act, 1949 would be amended to remove the lower and upper bounds to the SLR ratio, to allow banks to issue preference shares and to undertake consolidated supervision of banks and their subsidiaries.
- SEBI would be authorized to set up a National Institute of Securities Markets for teaching and training intermediaries in the securities markets and promote research.
- FIIs would be permitted to submit appropriate collateral when trading in derivatives on the domestic markets.
- Clear legal validity would be provided to the OTC derivatives.
- One time exemption from stamp duty on the national transfer of assets would be allowed to facilitate corporatization of stock exchange.
- Mumbai would be made regional hub for finance.
- Gold units would be introduced and traded in the same manner as units of mutual finds.

Other Proposals

- All States have agreed to introduce VAT from April 1, 2005. The States would be compensated according to an agreed formula.
- Allocation for Defence in 2005-06 is increased to Rs.83,000 crore from Rs.77,000 crore in 2004-05.
- A mechanism would be put in place to measure the development outcomes of all major programmes.
- The subsidy regime would be restructured in a continuous manner and after a thorough discussion.
- The year 2004-05 is expected to end with a revenue deficit of 2.7 per cent and a fiscal deficit of 4.5 per cent of GDP.

Budget Estimates

- Plan expenditure for 2005-06 is estimated at Rs.1,72,500 crore.
- Non Plan expenditure in 2005-06 is estimated to be Rs.3,70,847 crore.
- Revenue Receipts of the Central Government is estimated to be Rs.3,51,200 crore.
- Revenue expenditure is estimated at Rs.4,46,512 crore. Consequently, revenue deficit is estimated at Rs.95,312 crore which is equal to 2.7 per cent of the estimated GDP.
- The fiscal deficit is estimated as 4.3 per cent of the estimated GDP.