INDIA UPDATE

HIGHLIGHTS OF

UNION BUDGET 2007- 08

INDIABIZSOLUTIONS

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HIGHLIGHTS OF INDIAN UNION BUDGET FOR 2007-08

A. GENERAL:

- Improvement in GDP growth rate from 7.5% in 2004-05 to 9% (Quick Estimate) in 2005-06 and to 9.2% (Advance Estimate) in 2006-07; average growth rate in the last three years at 8.6%; growth target for the Tenth Plan of 8% will be nearly achieved; during three year period, acceleration in growth rate in manufacturing from 8.7% to 9.1% and further to 11.3%; and in services sector from 9.6% to 9.8% and further to 11.2%.
- Average growth in agriculture during Tenth Plan estimated at 2.3%.
- Income and Savings: Per capita income in 2005-06, in real terms, increased by 7.4%, savings rate estimated at 32.4% and the investment rate at 33.8%.
- Inflation: Growth in bank credit, year on year, by 29.6%; expansion in money supply (M3) by 21.3%; foreign exchange reserves at US$ 180 billion; pressure on domestic prices by global commodity prices; and supply constraints in some essential commodities - consequently, average inflation in 2006-07 estimated at between 5.2 and 5.4% as against 4.4% last year.
- Eleventh Five Year Plan Objectives: "Faster and More Inclusive Growth"; growth rate of approximately 10% by the end of plan period; growth of 4% in the agriculture sector, faster employment creation, reducing disparities across regions and ensuring access to basic physical infrastructure and health and education services to all.
- Allocations for Major Sectors: Increase in provision for Bharat Nirman by 31.6% from Rs.18,696 crore to Rs.24,603 crore, for education by 34.2% to Rs.32,352 crore & for health and family welfare by 21.9% to Rs.15,291 crore. Apart from various other allocations to various other sectors and social schemes: (i) Defence Expenditure: Allocation to increase to Rs.96,000 crore. (ii) Information Technology: Allocation for e-governance to increase from Rs.395 crore to Rs.719 crore and for e-governance action plans at State levels to increase from Rs.300 crore to Rs.500 crore; Rs.33 crore to be provided for a new scheme of manpower development for software export industry.
- Gross domestic capital formation in 2005-06 grew by 23.7 per cent; in April - January, 2006-07, foreign direct investment amounted to US$12.5 billion and outpaced portfolio investment of US$6.8 billion; Central Public Sector Enterprises to invest Rs.165,053 crore through internal and extra budgetary resources in 2007-08; Government to provide equity support of Rs.16,361 crore and loans of Rs.2,970 crore.
- Merchandise exports expected to cross US$125 billion by the end of the current fiscal.

- PAN to be made sole identification number for all participants in securities market with an alpha-numeric prefix or suffix to distinguish a particular kind of account;
- Mechanism to be put in place to permit Indian companies to unlock a part of their holdings in group companies by issue of Exchangeable Bonds for meeting their financing requirements.

- Institutions have been permitted to allow Delivery-based short selling and securities lending and borrowing to facilitate delivery
- Funds from National Small Savings Fund may also now be borrowed by India Infrastructure Finance Company Limited; suggestions of Deepak Parekh Committee to be examined for establishment of two wholly-owned overseas subsidiaries of IIFCL with objectives to (i) borrow funds from RBI and lend to Indian companies implementing infrastructure projects in India, or to co-finance their ECBs for such projects, solely for capital expenditure outside India; and (ii) borrow funds from the RBI, invest such funds in highly rated collateral securities and provide

'credit wrap' insurance to infrastructure projects in India for raising resources in international markets.

- Rs.110,268 crore of States' debt has been consolidated; twenty States have availed of benefit of debt waiver of Rs.8,575 crore; States' share of taxes & duties to increase from Rs.120,377 crore to Rs.142,450 crore; grants & loans to States and UTs to increase from Rs.90,521 crore to Rs.106,987 crore.
- Forward Contracts for wheat and rice to stop with immediate effect
- VAT, CST and a Roadmap towards GST: Agreement reached with State Governments to phase out CST; rate to be reduced from 4% to 3% with effect from April 1, 2007; Rs.5,495 crore provided for compensation for losses, if any, on account of VAT and also on account of CST; a roadmap for introducing a national level Goods and Services Tax (GST) with effect from April 1, 2010 to be prepared.

B. BUDGET ESTIMATES FOR 2007-08:

- Plan expenditure at Rs.205,100 crore; Non-Plan Expenditure (net of the SBI share acquisition) at Rs.435,421 crore with increase over 2006-07 of only 6.5%; **Revenue deficit estimated at Rs.71,478 crore (1.5% of GDP) and fiscal deficit at Rs.150,948 crore (3.3% of GDP).**

C. TAX PROPOSALS

Direct Taxes

The definition of the term "India" has been amended to include the air space above its territory and territorial waters.

Individuals:

- Threshold limit of exemption in the case of all assessees to be increased by Rs.10,000; in the case of a woman assessee, threshold limit to be increased from Rs.135,000 to Rs.145,000 and in case of a senior citizen from Rs.185,000 to Rs.195,000
- Deduction in respect of medical insurance premium under section 80D to be increased to a maximum of Rs.15,000 and, in case of a senior citizen, a maximum of Rs.20,000.
- Perquisite on account of concessional rent has been defined with retrospective effect from April 1, 2004
- Limit of Rs.50 lakh per investor per year with respect to capital gains bonds issued by NHAI and REC under section 54EC to continue.
- An additional cess of 1% on all taxes to be levied to fund secondary education and higher education
- In case, capital gain arises from the transfer of specified security or sweat equity shares, the value of which has been taken into account while computing the value of fringe benefits, the cost of acquisition of such security or shares shall be the fair value adopted for determining the fringe benefit.
- Interest paid on loans taken for higher education of spouse and children proposed to be deductible under section 80E.
- Capital Gains Tax shall be payable on the following items also since the same have been specifically excluded from the definition of the term "personal effects"
  (i) archaeological collections;
  (ii) drawings

(iii) paintings
(iv) sculptures or
(v) any work of art.

- Any individual or a Hindu undivided family, whose total sales, gross receipts or turnover from the business exceeds Rs.40 lacs or gross receipts in profession carried on by him exceeds Rs.10 lacs during the financial year immediately preceding the financial year in which such sum is credited or paid to the account of the contractor, then such individual or HUF shall be liable to deduct at source income tax at 1% in the case of advertising and 2% in other cases. Provided that no individual or a Hindu undivided family shall be liable to deduct income-tax on the sum credited or paid to the account of the contractor where such sum is credited or paid exclusively for personal purposes of such individual or any member of Hindu undivided family.
- TDS is proposed to be made applicable w.e.f. June 1, 2007in respect of interest exceeding Rs. 10,000 payable on 8% Savings (Taxable) Bonds 2003 during a financial year.

Corporate:

- No surcharge on income tax on all firms and companies with a total income of Rs.1 crore or less
- An additional cess of 1% on all taxes to be levied to fund secondary education and higher education. Accordingly, the total cess including the existing education cess would be 3% on all taxes.
- Minimum Alternate Tax (MAT) to be extended to income in respect of which deduction is claimed under sections 10A and 10B. Consequently STP & EOU units would be subject to MAT. MAT is not applicable to SEZ units.
- Rate of dividend distribution tax to be raised from 12.5% to 15% on dividends distributed by companies; and to 25% on dividends paid by money market mutual funds and liquid mutual funds to all investors.
- Weighted deduction available to a company engaged in the business of biotechnology or in the manufacture or production of drugs, pharma, electronic equipments, computers, telecom equipments etc in respect of expenditure on scientific research, in-house research and development is extended by another 5 years upto March 31, 2012.
- Pass-through status to be granted to venture capital funds only in respect of investments in venture capital undertakings in biotechnology; information technology relating to hardware and software development; nanotechnology; seed research and development; research and development of new chemical entities in the pharmaceutical sector; dairy industry; poultry industry; and production of bio-fuels, and hotel-cum-convention centres of a certain description and size.
- An Explanation is being added to Section 9 of The Income Tax Act to clarify with retrospective effect from June 1, 1976 that where income of the nature of interest, royalty and fee for technical services is deemed to accrue or arise in India, it shall be included in the total income of the non-resident, whether or not the non-resident has a residence or place of business or business connection in India.
- Deduction under section 36(1)(viii) to be restricted to 20% of profits each year.
- For availing benefits applicable to units Special Economic Zone, it has now been specified that in addition to the condition that the unit must have begun or begin to manufacture or produce articles or things or services during the previous year relevant to the assessment year commencing on or after the 1st day of April, 2006, the following conditions should also be complied with.

(i) it is not formed by the splitting up, or the reconstruction, of a business already in existence:

Provided that this condition shall not apply in respect of any undertaking, being the Unit, which is formed as a result of the re-establishment, reconstruction or revival by the assessee of the business of any such undertaking as is referred to in section 33B, in the circumstances and within the period specified in that section;

(ii) it is not formed by the transfer to a new business, of machinery or plant previously used for any purpose.

- Benefit of Section 36(1)(viii) to be available to cooperative banks; to be also allowed deduction in respect of provision for bad and doubtful debts under section 36(1)(viia); amalgamation and de-merger of banking companies is tax neutral - benefit to be extended to cooperative banks.
- Limit of Rs.50 lakh per investor per year with respect to capital gains bonds issued by NHAI and REC under section 54EC to continue.
- Tax holiday to undertakings in Jammu & Kashmir to be extended for another five years up to March 31, 2012.
- Concessions under section 80IA for infrastructure facilities to be extended to cross country natural gas distribution network, including gas pipeline and storage facilities integrated to the network; and to navigation channel in the sea.
- In the case of industrial undertakings or enterprises engaged in infrastructure development, etc. which are entitled to tax benefits under Section 80-IA, the tax benefit under Section 80-IA shall not be available when such enterprise or undertaking is transferred in a scheme of amalgamation or demerger on or after the 1st day of April, 2007.
- Benefit of carry forward of accumulated business loss and unabsorbed depreciation available to amalgamated company is proposed to be extended to public sector companies engaged in the business of operation of aircraft.
- To facilitate creation of urban infrastructure, issue of tax-free bonds through State Pooled Finance Entities formed for raising funds for a group of urban local bodies to be allowed.
- A five year income tax holiday for two, three or four star hotels and for convention centres with a seating capacity of not less than 3,000; they should be completed and begin operations in National Capital Territory of Delhi or in the adjacent districts of Faridabad, Gurgaon, Ghaziabad or Gautam Budh Nagar during April 1, 2007 to March 31, 2010.
- Where any expenditure in respect of which payment is made in a sum exceeding twenty thousand rupees otherwise than by an account payee cheque drawn on a bank or account payee bank draft, no deduction shall be allowed in respect of such expenditure instead of 20% of such expenditure
- A benign assessment procedure to be introduced for assessees engaged in diamond manufacturing and trading who declare profits from such activities at 8% or more of turnover.
- The time limit for completion of assessment / reassessment is proposed to be increased by twelve months wherever reference is made to the TPO for determination of arm’s length price. It is also proposed that the TPO would determine the arm’s length price at least sixty days before the expiry of new statutory time limit for making the assessment / reassessment.
- It has been now provided that the Assessing Officer shall compute the total income of the assessee under sub-section (*4*) of section 92C in conformity with the arm’s length price as so determined by the Transfer Pricing Officer and therefore, unlike earlier, no discretion is available to the Assessing Officer

- Provision of appeal by a person denying liability to deduct tax under section 195 of the Act is proposed to be restricted to person who has paid the tax deductible on income of the non-resident under ‘net of tax’ arrangement and who is denying that any tax was deductible. The prescribed time shall be counted from the date of payment of tax.
- Appellate Tribunal is proposed to be empowered to grant stay for a period not exceeding one hundred and eighty days and where the appeal is not disposed off within the said period the Appellate Tribunal may further extend the period(s) not exceeding in aggregate three hundred and sixty five days. The stay would stand vacated after the expiry of such period where the appeal is not disposed off.
- An order holding a person as an assessee in default under section 206C(6A) shall be appealable before the Commissioner (Appeals)
- An opportunity of being heard is proposed to be given to the assessee before directing a special audit of its accounts
- The expenses on such special audit to be determined by the Chief Commissioner/Commissioner of Income Tax and paid by the Central Government
- The rate at which tax is to be deducted at source in respect of commission & brokerage and fees for professional and technical services has been increased from 5% to 10% with effect from 1st June 2007.
- The rate at which tax is to be deducted at source in respect of rent with effect from 1st June 2007 shall be as follows:
    (i) ten per cent. for the use of any machinery or plant or equipment;
    (i) fifteen per cent. for the use of any land or building (including factory building) or land appurtenant to a building (including factory building) or furniture or fittings where the payee is an individual or a Hindu undivided family; and
    (i) twenty per cent. for the use of any land or building (including factory building) or land appurtenant to a building (including factory building) or furniture or fittings where the payee is a person other than an individual or a Hindu undivided family.
- The provisions relating to proceedings before the Settlement Commission have been amended.

Fringe Benefit Tax:

- Expenditure on free samples and on displays to be excluded from the scope of Fringe Benefit Tax (FBT);
- ESOPs brought under FBT. The fair market value of the specified security or sweat equity shares referred to in clause (*d*) of sub-section (*1*) of section 115WB, on the date of exercise of the option by the employee as reduced by the amount actually paid by, or recovered from the employee in respect of such security or shares shall be considered as fringe benefit. For the purposes of this clause, “fair market value” means the value determined in accordance with the method as may be prescribed by the CBDT.
- Advance tax on the current fringe benefits shall be payable by –
  (*a*) all the companies, who are liable to pay the same in four instalments during each financial year and the due date of each instalment and the amount of such instalment shall be as specified in Table given below:

Due date of instalment	Amount payable
On or before the 15th June	Not less than fifteen per cent. of such advance tax.
On or before the 15th September	Not less than forty-five per cent. of such advance tax as reduced by the amount, if any, paid in the earlier instalment.
On or before the 15th December	Not less than seventy-five per cent. of such advance tax as reduced by the amount or amounts, if any, paid in the earlier instalment or instalments.
On or before the 15th March	The whole amount of such advance tax as reduced by the amount or amounts, if any, paid in the earlier instalment or instalments;

(*b*) all the assessees (other than companies), who are liable to pay the same in three instalments during each financial year and the due date of each instalment and the amount of such instalment shall be as specified in Table given below:

Due date of instalment	Amount payable
On or before the 15th September	Not less than thirty per cent. of such advance tax
On or before the 15th December	Not less than sixty per cent. of such advance tax as reduced by theamount or amounts, if any, paid in the earlier instalment or instalments.
On or before the 15th March	The whole amount of such advance tax as reduced by the amount or amounts, if any, paid in the earlier instalment or instalments;

- Where an assessee has failed to pay the advance tax payable by him on or before the due date for any instalment or where the advance tax paid by him is less than the amount payable by the due date, he shall be liable to pay simple interest at the rate of one per cent. of the amount by which the advance tax paid falls short of the amount payable by the due date for every month or part of the month for which the shortfall continues.

BCTT:

- Cash withdrawals by Central and State Governments to be excluded from the scope of Banking Cash Transactions Tax (BCTT);
- Exemption limit for individuals and HUFs to be raised from Rs.25,000 to Rs.50,000.

Indirect Taxes:

Customs duties:

- Reduction in peak rate for non-agricultural products from 12.5% to 10%.
- Reduction in duty on most chemicals and plastics from 12.5% to 7.5%; on seconds and defectives of steel from 20% to 10%.
- All coking coal irrespective of ash content to be fully exempt.
- Reduction in duty on polyester fibres and yarns from 10% to 7.5% and on raw-materials such as DMT, PTA and MEG from 10% to 7.5%; on cut and polished diamonds from 5% to 3%; on rough synthetic stones from 12.5% to 5%; and on unworked corals from 30% to 10%.

- Dredgers to be fully exempt from import duty.
- Reduction in duty on drip irrigation systems, agricultural sprinklers and food processing machinery from 7.5% to 5%.
- Reduction in general rate of import duty on medical equipment to 7.5%.
- Crude and refined edible oils to be exempt from additional CV duty of 4%; reduction in duty on sunflower oil, both crude and refined, by 15 percentage points.
- Reduction in duty on pet foods from 30% to 20%; on watch dials and movements and umbrella parts from 12.5% to 5%; to promote research and development, concessional rate of 5% duty to be extended to all research institutions registered with the Directorate of Scientific and Industrial Research; reduction in duty from 7.5% to 5% on 15 specified machinery for pharmaceutical and biotechnology sector.
- Duty of 3% (WTO bound rate) to be levied on all private import of aircraft including helicopters; such import to also attract countervailing duty and additional customs duty.
- Export Duty of Rs.300 per metric tonne to be levied on export of iron ores and concentrates and Rs.2,000 per metric tonne on export of chrome ores and concentrates.
- Section 14 of the Customs Act, 1962 is proposed to be amended to provide that the value of imported goods and exported goods shall be the transaction value of such goods. It is further proposed to provide that the transaction value in case of imported goods shall include any amount that the buyer is liable to pay for cost and services, including commissions and brokerage, assists, engineering, design work, royalties and license fees, costs of transportation to the place of importation, insurance and handling charges.

- Refund provisions are being amended to provide that the relevant date for the purpose of filing a refund claim in consequence of any judgment of an adjudicating authority would be the date of such a judgment.

- Advance Ruling provisions are being amended to explain that a joint venture in India means a venture in which at least one of the participants, partners or equity holders is a non resident having substantial interest in the joint venture and exercising joint control over it.

- The provisions relating to proceedings before the Settlement Commission have been amended.

Excise Duties:

- Reduction in ad valorem component of excise duty on petrol and diesel from 8% to 6%.
- Exemption limit for small scale industry (SSI) to be raised from Rs.1 crore to Rs.1.5 crore;
- Biscuits whose retail sale price does not exceed Rs.50 per kilogram and all kinds of food mixes including instant mixes to be fully exempt;
- Reduction in duty on umbrellas and parts of footwear from 16% to 8%
- Reduction in duty on plywood from 16% to 8%;
- Biodiesel to be fully exempt.
- Water purification devices operating on specified membrane based technologies and domestic water filters not using electricity to be fully exempt; exemption on pipes used for carrying water from a water supply plant to a storage facility to be extended to all pipes of diameter exceeding 200 mm used in water supply systems.
- Excise Duty to be fully exempt in respect of DVD drive & flash memory

- Reduction in the rate of duty from Rs.400 per metric tonne to Rs.350 per metric tonne on cement sold in retail at not more than Rs.190 per bag; rate of Rs.600 per metric tonne on cement that has a higher MRP.
- Excise duty reduced from 16% to 12% on caprolactum, Nylon & benezene used for manufacture of caprolactum
- Specific rates of duty on cigarettes to be increased by about 5%; duty (excluding cess) on biris to be raised from Rs.7 to Rs.11 per thousand for non-machine made biris and from Rs.17 to Rs.24 per thousand for machine made biris
- Duty on pan masala not containing tobacco to be reduced from 66% to 45%
- Withdrawal of exemption for pan masala containing tobacco and other tobacco products given to units in the North Eastern States.
- Withdrawal of exemption in respect of recorded video cassettes intended for television broadcasting, supplied in formats such as U- matic, Betacam or any similar format, etc.
- MRP based assessment is being extended from a date to be notified to personal computers (including laptops and other portable computers), printers, monitors, computer key boards, scanners, computer mouse, facsimile machines, modems, set top boxes for gaining access to internet and television sets.
- E-payment made mandatory for payment of duty by all assessees who have paid excise duty of Rs.50 lakh or more in cash during the preceding financial year.
- Section 11B of the Central Excise Act, 1944 amended to provide that the relevant date for the purpose of refund of duty in consequence of a judgment, decree, order or direction of appellate authority, Appellate Tribunal or any court, shall be the date of such judgment, decree, order or direction.
- Relevant changes made in Valuation Rules to provide that where goods are manufactured by a job-worker on behalf of a person (principal manufacturer), the value for payment of excise duty would be based on the sale value at which the principal manufacturer sells the goods, as against the earlier provision which provided that the value would be the cost of raw materials plus the job charges.

Service tax:

- **Basic Exemption:** Exemption limit for small service providers to be raised from Rs.400,000 to Rs.800,000
- **Extension of service tax to:**
  - services outsourced for mining of mineral, oilor gas;
  - renting of immovable property for use in commerce or business (residential properties, vacant land used for agriculture and similar purposes, and land for sports, entertainment and parking purposes & immovable property for educational or religious purposes to be excluded);
  - development and supply of content for use in telecom and advertising purposes;
  - asset management services provided by individuals;
  - design services;
  - services involved in execution of a works contract with an optional composition scheme under which tax will be levied at only 2% of the total value of works contract.
- **Exemption from Service Tax to:**
  - Services provided by Resident Welfare Associations to their members who contribute Rs.3000 or less per month for services rendered

- services provided by technology business incubators, their incubatees whose annual business turnover does not exceed Rs.50 lakhs to be exempt for first three years;
- clinical trial of new drugs

- Department of Telecommunications to constitute a committee to study the present structure of levies on telecom industry.
- Rules have been amended to provide self-adjustment of excess service tax paid, subject to specified conditions
- Rules have been amended to allow rectification of mistakes for and filing revised returns within 60 days from the date of submission of original return, subject to specified conditions
- Rules have been amended to enable submission of self-attested copy of the original registration certificate instead of original registration certificate while intimating any changes
- Rules have been amended to restrict the payment of service tax under reverse charge mechanism in relation to sponsorship service where the recipient of service is located in India

CST:

- CST rate to be reduced from 4% to 3% with effect from 1st April 2007
- List of declared goods under section 14 of the CST Act to be amended to cover all small aircraft with minimum takeoff mass of less than 40,000 kgs operated by scheduled airlines.

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