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ADVOCATES AND LEGAL CONSULTANTS

KEY FEATURES

OF UNION BUDGET 2012-2013

ECONOMIC OVERVIEW:

During the beginning of financial year 2011-2012, the Indian economy presented sign of recovery from the global meltdown started in late 2008 but this recovery was interrupted due to various issues such as intensification of debt crises in euro zone, political turmoil in middle east, rise in crude oil prices, threats of conflict between Israel and Iran and earthquake in Japan. The macro-economic factors like inflationary trend, lack of liquidity in the system, high interest rates and concerns relating to fiscal deficit also marred the economic recovery.

Global economic environment such as downgrading of, U.S. government's sovereign credit rating, banks and credit societies in Europe, entire Indian banking system and downgrading of France and eight other euro-zone countries on their sovereign debt further stalled the recovery of the Indian economy.

During the financial year 2011-2012, the Gross Domestic Product ("GDP") growth is estimated at 6.9% as compared to 8.4% during previous two financial years. However during the financial year 2012-13, India's GDP is expected to accelerate at 7.6% with falling inflation and fiscal consolidation.

BUDGET PROPOSALS:

In the present hostile economic situation, the Finance Minister had to present the budget capable of managing growth with price stability. Some of the tax proposals in the budget are guided by Direct Tax Code ("DTC") in case of direct taxes and Goods and Services Taxes ("GST") with reference to indirect taxes.

Overall the budget attempts to do a balancing act with a focus on structural reforms. Nevertheless, on one hand, the common man, hard-pressed by inflation, also has some reasons to cheer on revisions in income tax exemption limit, however the cheer, on the other hand, shall prove very short lived because of an upward revision in service tax and other indirect taxes which are likely to affect purchasing power of aam-admi.

The budget proposes to introduce advance price mechanism for Transfer pricing. The budget also proposes to rationalize the law relating to tax treatment to the venture capital funds and negative impact of dividend distribution tax in multi layered corporate structures. The Government also wants to widen the scope the service tax wherein all services except those listed in negative list shall be under the tax net.

The budget also proposed to introduced General Anti Avoidance Rules ("GAAR") to counter aggressive tax avoidance and further various other measures have been proposed to deter generation and use of black money. The uncertainty of GAAR had spooked stock markets on concerns that all short-term capital gains made by Foreign Institutional Investors ("FIIs") and participatory note investments would be taxed. The Finance Minister Mr. Pranab Mukherjee clarified that investments through participatory notes would not face any tax on capital gains in India. Further finance ministry has also clarified that FIIs based in Mauritius will not be required to pay capital gains in India if they have 'substantial commercial interest' in the island nation. But the FIIs are not convinced with the explanations and presently engaged in evaluating their new tax risks.

Unfortunately, the budget also proposes retrospective amendment in Income Tax Act with intention to levy tax on capital gains arising on the sale of shares between two foreign entities linked to underlying assets in India. This is likely to have adverse impact on stability of tax policies in India. It would shore up tax compliance costs for corporate investments and almost certainly affect investor confidence.

In this article, we are briefly referring the budget proposals with analysis of few important issues to make it more informative and expressive.

KEY POLICY ANNOUNCEMENTS:

(i). Rationalization of key policies:

- **Amendment to the** Fiscal Responsibility and Budget Management **('FRBM')** Act – The concept of "Effective Revenue Deficit" and "Medium Term Expenditure Framework" statement are two important features of amendment to FRBM Act. This will help in reducing consumptive component of revenue deficit and create space for increased capital spending.
- **Central Plan Scheme Monitoring System** to be expanded for better tracking and utilization of funds.
- **DTC Bill** to be enacted at the earliest after examination of the report of Parliamentary Standing Committee.
- **GST network** to be set-up as National Information Utility and shall be operationalized by August 2012.
- **White Paper on Black Money** to be presented in Parliament.
- **Legislative measures** for strengthening **anti-corruption framework** are at various stages of enactment.
- **National Food Security Bill, 2011** is presently before Parliamentary Standing Committee for their review.
- Bill regarding **Public Procurement Legislation** to be introduced in Parliament to combat corruption.

(ii). Subsidies:

- To **keep subsidies below 2% of GDP** during F.Y. 2012-13 and further bring it down to 1.75% of GDP in the next 3 years.
- To roll out Nation-wide mobile-based **Fertilizer Management System** to provide complete information on movement of fertilizers and subsidies.
- Endeavour to scale up and **roll out Aadhaar enabled payments** for various government schemes in at least 50 districts within next 6 months.

(iii). Disinvestments

- During the F.Y. 2012-13, the **disinvestments** target, from sale of shares of public sector undertakings, has been set at **Rs. 30,000 crore;** however 51% ownership and management control shall remain with the Government.

(iv). Infrastructure:

- During Twelfth Plan period, investment in infrastructure to go up to Rs. 50 lakh crore. The half of this amount is expected from private sector.
- Approved guidelines to establish **joint venture companies** in PPP mode by defense PSUs.
- **Tax free bonds of Rs 60,000 crore** for financing infrastructure projects in FY 2012-13.
- Allocation under Rural Infrastructure Development Fund enhanced to Rs. 20,000 crore. Rs. 5,000 crore earmarked exclusively for creating warehousing facilities.

(v). Financial Sector

- Introduction of Rajiv Gandhi Equity Saving Scheme which allows income tax deduction of 50% to new retail investors to invest up to Rs. 50,000 directly in equities.The retail investors should have annual income below Rs.10 lakh.
- Rs 15,888 crores proposed for capitalization of public sector banks and financial institution

(vi). Agriculture

- Target for **agriculture credit flow** to increase by Rs. 1, 00,000 crore to **Rs 5,75,000 crore**.
- **Interest subvention scheme on short term crop loan** to continue at **7%** p.a. Additional subvention of **3%** available for prompt payments. Kisan Credit Card shall be modified to use it as a smart card.
- A sum of Rs. 200 crore provided **for incentivizing Agricultural Research with rewards**.
- **Regional Rural Bank credit refinance fund** shall be set-up for disbursing **short-term crop loans to small and marginal farmers.**

- A new centrally sponsored scheme titled **"National Mission on Food Processing"** to be started in F.Y. 2012-13 in co-operation with State Governments.

(vii). Textile Sector

- Financial stimulus of **Rs 3,884 crore** for waiver of loans of handloom weavers.
- Two more mega handloom clusters to be set up in Andhra Pradesh and Jharkhand.
- Rs. 500 crore pilot scheme for promotion and application of Geo-textiles in the North Eastern Region.
- A power loom mega cluster shall be set up at Ichalkaranji in Maharashtra with allocation of Rs.70 crore.

(viii). Power and Coal Sector

Coal India Limited advised to **sign fuel supply agreements** with power plants, having long-term PPAs with distribution companies and getting commissioned on or before 31st March, 2015.

(ix). Transport Sector

- Target of covering a length of 8,800 Kms under NHDP.
- **Road Transport and Highways Ministry allocation** enhanced by 14% to **Rs 25,360 crore.**
- Assistance of Rs. 18,500 crore spread over 5 years for construction of **Delhi Mumbai Industrial Corridor** approved with the **Japanese participation of USD 4.5 billion in the project.**
- **Direct import of Aviation Turbine Fuel** for Indian carriers permitted.
- Equity **participation of foreign airlines** in airlines undertaking **up to 49%** is under consideration. **ECB** of **USD 1 billion** to be permitted for 1 year in respect of working capital requirements of airline industry.

(x). Micro, Small and Medium Enterprises

- **India Opportunities Venture Fund** of **Rs 5,000 crore** to be set up with SIDBI.
- Ministries and Central Public Sector Enterprises to make a **minimum of 20% of their annual purchases** from MSMEs. The **4% of total purchases** have been earmarked from **MSMEs owned by SC/ST entrepreneurs.**

(xi). Education, Employment and Healthcare

- Allocation for **Sarva Shiksha Abhiyan** enhanced by 21.7% to Rs 25,555 crore in FY 2012-13
- **6,000 schools** proposed to be set up at block level as model schools in Twelfth Plan.
- To ensure better flow **of credit to students**, a Credit Guarantee Fund proposed to be set up.
- Bring greater synergy between MGNREGA, agriculture and allied rural livelihoods.
- Allocation for **National Rural Livelihood Mission** increased by 34% to **Rs 3,915 crore.**
- **Prime Minister's Employment Generation Programme** allocation enhanced by 23% to Rs 1,276 crore.
- Allocation of **Rs 1,000 crore** for **National Skill Development Fund** in FY 2012-13.
- Allocation for **National Rural Health Mission** to **Rs 20,882 crore** in FY 2012-13.

  National Urban Health Mission to be launched in FY 2012-13 to meet the health needs of the urban poor.

(xii). Budget Estimates

- **Gross Tax Receipts** estimated at **Rs 1,077,612 crore** for FY 2012-13
- **Total expenditures** budgeted at **Rs 1,490,925 crore** for FY 2012-13
- **Fiscal deficit** at 5.1 per cent of GDP in 2012-13.

  Net market borrowing required to finance the deficit to be **Rs. 4.79 lakh crore** in 2012-13.

TAX PROPOSALS:

DIRECT TAX:

Personal tax:

Personal income-tax slabs proposed to be revised as under:

Existing Slab (Rs.)	Revised Slab (Rs)	Tax Rate (%)
Upto 180,000	Upto 200,000	NIL
180,001 to 500,000	200,001 to 500,000	10
500,001 to 800,000	500,001 to 1,000,000	20
Above 800,000	Above 1,000,000	30

Proposed slab rates in line with DTC Bill, 2010.

- Exemption limit for individuals (other than senior citizen) increased to Rs. 200,000.
- No differentiation for basic exemption limit for women. Accordingly, the additional benefit to women is lowered by Rs.1,000.
- Limits remain unchanged for senior citizens (age of 60 years and above but less than 80 years) at Rs. 250,000.
- Limits remain unchanged for very senior citizen (age of 80 years and above) at Rs 500,000.
- Education Cess and Secondary and Higher Education Cess at 2% and 1% respectively to continue.
- Any sum received under a life insurance policy is exempt from tax, provided the premium payable for such policy for the year does not exceed 10% of the sum assured.
- Deduction of Rs. 15,000 under Section 80D has been broadened to include expenditure of Rs. 5000/- on preventive health check-up.
- Exemption of Rs. 10,000 is available for interest earned on deposits in savings bank account, co-operative banks and post office.
- Exemption available for capital gains on sale of residential property (house or land) where the net-consideration is invested in a small and medium enterprise (SME) subject to specified conditions.
- TDS at the rate of 1% on transfer or certain immovable properties (other than agricultural land).

Corporate tax

- No change in base corporate tax rate for domestic and foreign companies and DDT.
- No change in surcharge and cess.
- Effective tax rates are as below:

  For domestic companies, where income exceeds Rs. 1 crore - 32.445%, where income is less than Rs.1 crore – 30.6%.
- **For foreign companies**, where income exceeds Rs. 1 crore – 42.024%, where income is less than Rs.1 crore – 41.2%.
- Concessional rate of 15% for dividend received from foreign subsidiary has been extended by 1 more year.
- Securities Transaction Tax ('STT') on actual delivery or transfer of shares reduced from the existing 0.125% to 0.1%.
- Interest income paid by specified companies (infrastructure companies like construction of road, toll road or bridge and power etc.) to a non-resident shall be subject to concessional withholding tax rate of 5%.
- Venture capital benefit is available to all funds without any restrictions. Existing sectoral restrictions have been removed.
- Weighted deduction of 200% for in-house research expenditure has been extended for a further period of 5 years till 31st March, 2017.
- The budget also proposes changes/introduction in/ of Minimum Alternate Tax (MAT), Alternate Minimum Tax (AMT), General Anti-Avoidance Rule (GAAR), retrospective amendments in Income Tax Act, Condition to avail benefits under the tax treaty and Advance Pricing Arrangement etc.

INDIRECT TAX:

Customs:

- Peak rate of Customs Duty maintained at 10%.
- Customs duty exemption on specified equipments extended to all infrastructure projects.
- Rate of Basic Customs Duty (BCD) on capital goods for setting up / expansion of Iron ore plants reduced from 7.5% to 2.5%.
- Exemption from BCD for setting up/expansion of fertilizer projects extended till 31st March 2015.
- Full exemption from BCD extended to equipments for coal mining projects and LCD/LED TV panels
- Duty free limit on articles accompanying passengers increased from Rs. 25,000/- to Rs. 35,000/-.

Excise:

- Standard rate of Excise duty on non- petroleum goods increased from 10% to 12%.
- Excise duty of 2% on spare parts of mobile phones without CENVAT credit.
- Merit rate for non –petroleum goods increased from 5% to 6% and rate of 1% on certain items imposed in the previous Budget increased to 2%.
- Cement/Cigarettes to be assessed on Specific –cum-ad-valorem basis (Retail Sale Price (RSP)). Abatement on RSP also notified.
- Abatement of RSP on readymade Garments and made up articles of textiles increased from 55% to 70% of RSP.
- Duty on Eco-friendly products like electric/hybrid vehicles and LED lamps reduced to 6%.
- Facility to transfer unutilized Cenvat Credit of Special Additional Duty from one factory to another of the same manufacturer.
- Interest on credit wrongly taken is not payable unless the same is utilized.

Service Tax

- Service tax rate increased from 10% to 12%.
- Paradigm shift in the manner of taxation of services. As against the present system of defining the taxable services, it is proposed to define the services that are not taxable (Negative list approach introduced).
- Excess service tax paid can be adjusted without any monetary limit.
- Penalty is waived if Service tax for the past period in respect of Renting of Immovable Property service is paid along with interest within 6 months.
- Time limit for issuing show cause notice increased from 12 month to 18 months.

Central Sales Tax

- No changes in CST. CST continues at 2% with Form C.

CONCLUSION:

Budget was presented against a backdrop of a tricky fiscal situation and concerns of the revival of domestic growth prospects. The Government very categorically conveyed that it will be a forward looking budget, which would control inflation, provide thrust to the industrial sectors and provide relief to common man. But unfortunately, the budget has proved to be a painful pill with Service Tax being extended to all services and further 2% hike in the Service Tax and Central Excise rates could further lead to price rise across the board.

The proposal has been made to tax indirect transfer of capital assets in India by retrospectively amending the Income Tax Act from the F.Y. 1961-62. This amendment has primarily been proposed to reverse the judgment of Supreme Court in Vodafone case. The legal experts are divided over the validity of this amendment and same is certainly going to be challenged in court of law, thus it will further add to uncertainty among the prospective investors.

GAAR the most obnoxious part of the Direct Taxes Code has been implemented. Now, it shall be presumed that obtaining of tax benefit is the main purpose of an arrangement unless otherwise proved by the taxpayer. GAAR is primarily being criticized because of granting discretion and authority to the tax administration which, at times, is prone to be misused.

The commitment of government to reduce fiscal deficits is laudable. The increased spending on infrastructure, health, education, employment and social schemes is need of the hour with caution to ensure delivery in organized manner. The government's efforts to achieve consensus on GST and intention of early introduction of DTC are praise worthy. The government's initiatives in making consensus among all political parties and other stake holders will pave way for new beginning in economic reforms to make India as vibrant and robust economy.

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