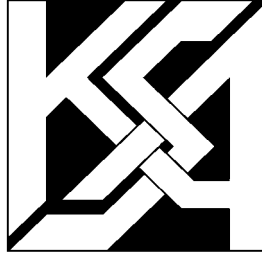


UNION BUDGET 2004 – AN OVERVIEW



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① INTRODUCTION

In the general elections held in 2004, the people of India voted in favour of change of the government at the centre. As a result, the new coalition government under the leadership of the Prime Minister, Dr. Manmohan Singh, assumed power in May 2004. This government has been formed by a number of political parties led by Congress as United Progressive Alliance (UPA). Though the parties forming UPA have different ideologies as to the economic policies, for the purpose of smooth and cohesive governance, they have evolved a common understanding which is documented as the National Common Minimum Programme (NCMP).

The Hon'ble Finance Minister, Mr. P. Chidambaram, presented the Union Budget for the fiscal year 2004-05 before the Parliament on 8th July, 2004 along with the Finance (No. 2) Bill, 2004 containing the tax proposals. The NCMP laid down the basic grounds on which Mr. Chidambaram formulated this maiden budget of UPA. Issues like agricultural and rural development, employment generation, basic education and health, dominated the policies underlying the formulation of budget. This budget sends an important signal that though the government comprises of powerful regional political parties and is supported by the leftist parties from outside, the process of economic reforms and liberalization continues without any interruption.

The Indian economy has continued its good performance in fiscal year 2003-04 also and undergone significant structural changes due to the ongoing economic reforms. The Central Government started divesting its stake in a number of PSUs at the fag end of the year. Foreign Institutional Investors invested heavily in the country. The capital markets remained buoyant during a major part of the year. The GDP growth rate is estimated to be over 8% as against 4% in the previous year. The buoyancy was visible in most sectors of the economy; agriculture grew over 9%, manufacturing 6.5% and services around 8.4%. Inflation was also kept below 5%. Foreign exchange reserves stood at Rs.113 billion (US \$ 2.57 billion) as of March 2004. This indicates that the Indian economy is in a healthy situation. Therefore, it seems it is now time to identify the weaker part of the Indian economy which did not flourish in spite of economic reforms over several years. The political parties in the opposition at the time of the general elections clearly identified this weakness and got the backing of the masses to come to power. This agenda then embedded itself in the NCMP and has become a basis for formulating policy as announced through this budget.

This Budget, as declared by the Hon'ble Finance Minister, has the following objectives:

- ❖ Sustained GDP Growth of 7-8%
- ❖ Improve the quality of health, education, and generate rural employment
- ❖ Focus on Agriculture and rural infrastructure
- ❖ Enhancing investment in industry, both public and private, domestic and foreign



- ❖ Encouraging savings and protecting the savings of the senior citizens.
- ❖ Developing infrastructure with special focus on water, port, and aviation.

To fulfill the above objectives, this budget has proposed the following major initiatives:

- ⇒ Additional budgetary support of Rs. 10,000 crores (US \$ 2.27 billion) for planned expenditure for the year 2004-05 to fund various development activities especially in rural areas.
- ⇒ Doubling agricultural credits in three years, accelerating the completion of irrigation projects and investing in rural infrastructure.
- ⇒ Allocation of funds for farm, live stock insurance and health insurance to poor section of the society.
- ⇒ Allocation of resources for drinking water.
- ⇒ Investment in public sector undertakings in core sector like petroleum, aviation etc.
- ⇒ Higher FDI limit in aviation, insurance and telecommunication sector.
- ⇒ Proposal for creation of Investment Commission in addition to Foreign Investment Promotion Board with a view to form policies to attract investments, both domestic and foreign.
- ⇒ Development of capital markets with higher inflow from FII and Banking sector.
- ⇒ Easy access to small and medium enterprises to the capital market.
- ⇒ Steps for integration of commodities market and securities markets.
- ⇒ Implementation of VAT with effect from April, 1, 2005.
- ⇒ Amendments to be made in Securitisation Act, to ensure speedy recovery of NPAs (Non-Performing Assets).
- ⇒ Proposal to introduce Special Economic Zone Bill.

The budget estimate of fiscal deficit for the fiscal year 2004-05 stands at 4.4% of GDP as against 4.6% as per the revised estimate for the fiscal year 2003-04. In absolute terms, the total fiscal deficit is estimated at Rs. 137,407 crores (US \$ 31.22 billions) for the year 2004-05.

This booklet is meant to apprise our esteemed clients of the important budget proposals mainly in the field of direct taxes while an attempt has been made to cover the indirect taxes also. We offer a broad outline of the major proposals.

The changes proposed in the Finance Bill become effective from Assessment Year(A.Y.) 2005-06, i.e. the financial year beginning on 1st April, 2004, unless otherwise stated.



② BUDGET HIGHLIGHTS

Direct Taxes

- ✓ No change in basic income tax rate structure.
- ✓ No tax payable in the case of Individuals having taxable income upto Rs. 1,00,000/-
- ✓ New Education cess at 2% on Income Tax, Excise Duty, Custom Duty and Service Tax levied in all cases.
- ✓ New optional tonnage tax scheme introduced for shipping companies.
- ✓ Abolition of tax exemption on interest earned by NRE Account.
- ✓ Long Term Capital Gains on Securities traded on recognized stock exchanges abolished and Short Term Capital Gains on such securities to be taxed at 10%.
- ✓ Securities transaction tax levied on all buyers at 0.15 % on such transaction value of securities.
- ✓ Gifts (excluding marriage gift) received from unrelated persons over Rs. 25,000/- (US \$ 568) to be taxed as income.
- ✓ Deduction of 100% of profits for 5 years and 25% of profits for the next 5 years to be allowed in the case of new agro-processing industries set up to process, preserve and package fruits and vegetables.
- ✓ Additional depreciation of 15% allowed on new plant and machinery acquired and installed in an existing undertaking to continue with the required increase in installed capacity at 10% instead of 25%.
- ✓ Automobile industry to be notified as an industry entitled to 150% deduction of expenditure on in-house R & D facilities.
- ✓ Benefit under section 80 IA to be extended to power sector projects undertaken during the period 1st April, 2004 to 31st March, 2006.
- ✓ Benefit under section 80 IB to be extended to new hospitals with 100 beds or more set up in rural areas; such hospitals to be entitled to a 100% deduction of their profits for a period of five years.
- ✓ Benefits to the housing industry under section 80 IB extended to the projects approved before 31st March, 2007.



- ✓ Open-ended equity oriented mutual funds to continue to be exempt from distribution tax on dividends; rate of tax on corporate unit holders of debt-oriented mutual funds to be raised to 20% with no change for individuals and HUF unit holders.
- ✓ Benefits to the telecom sector under section 80 IA for services commenced before 31st March, 2004 - terminal date to be extended to 31st March, 2005.
- ✓ 100% deduction of profits for 10 years to companies carrying on scientific research and development approved by the Department of Scientific and Industrial Research before 1st April, 2004 - terminal date to be extended to 31st March, 2005.
- ✓ 100% tax exemption to new industrial undertakings in Jammu and Kashmir if they commenced production before 31st March, 2004 – date to be extended to 31st March, 2005.

Indirect Taxes

- ✓ Removal of exemption from CVD enjoyed by some imported goods where there is no corresponding exemption from excise duty on Indian made goods.
- ✓ Custom duty on non-alloy steel to be reduced from 15% to 10% and excise duty on steel to be increased from 8% to 12% so that the countervailing duty will also be applicable to imports.
- ✓ Peak rate on alloy steel, copper, lead, zinc and base metals to be reduced to 15%; customs duties on refractory raw minerals and mineral products like graphite, asbestos, mica and gypsum to be reduced to 15%; custom duty on all catalysts also to be 15%.
- ✓ Tractors, dairy machinery and hand tools such as spades, shovels, sickles, etc. which attract a 16% excise duty to be fully exempt.
- ✓ Excise duty to be reduced from 16% to 8% on preparations of meat, poultry and fish and from 32% to 16% on food grade hexane (used in the edible oil industry).
- ✓ Specified raw materials for manufacture of parts of cathode ray tubes and specified capital goods for manufacture of mobile handsets, plasma display panels, etc. to be exempt from excise duty; specified items for manufacture of telecom grade optical fibres and cables to be exempt from custom duty; custom duty exemption to be extended to imports by universal access service providers.
- ✓ Full excise duty exemption to be granted on computers; some excise relief to be given to LPG gas stoves bearing an MRP upto Rs. 2,000/ (US \$ 45), footwear with MRP upto Rs. 250/- (US \$ 6) and writing instruments with MRP upto Rs.200/- (US \$ 5).



- ✓ Concessional custom duty of 5% on capital goods to be extended to the non-leather footwear industry; patent leather to be exempt from custom duty.

Service Tax

- ✓ Credit of service tax and excise duty to be extended across goods and services; rate of service tax to be enhanced from 8% to 10%; addition of some more new services; mandatory departmental verification of self-assessment and the penalty for non-registration to be done away with.

③ DIRECT TAX PROPOSALS

3.1 TAX RATES :

The Finance (No. 2) Bill, 2004 does not envisage any change in the basic rate of corporate and personal income tax. Accordingly, the rate applicable for A. Y. 2004-05 would continue to apply for A. Y. 2005-06. However, the levy of education cess on income tax at 2% on income tax (including surcharge, wherever applicable) would result in increasing the effective tax rate marginally.

However, in case of resident individuals having taxable income upto Rs. 1,00,000/- (US \$ 2,273) no income tax will be payable in view of tax rebate u/s. 88D which is equivalent to 100% of tax payable.

The effective rate of corporate tax for A. Y. 2005-06 works out to 36.59% as against the present rate of 35.875%. In case of foreign companies, the effective tax rate for A. Y. 2005-06 works out to 41.82% as against the present rate of 41% (unless a separate treatment is provided for in the relevant tax treaties). The maximum marginal rate of tax in case of individual tax payers (where the total income exceeds Rs. 8,50,000/- (US \$ 19,318)) would be 33.66% for A. Y. 2005-06 as against the existing rate of 33%.

3.2 NEW TAX INCENTIVES AND RELIEFS :

a) *Taxation of capital gains from listed securities:*

A new clause (38) is proposed to be inserted in section 10 of the Income-tax Act, 1961 to exempt long term capital gain arising on sale of securities in a recognized stock exchange in India where such sale is effected on or after the date to be notified by the Central Government on which the securities transaction tax will come into force ("notified date"). This exemption is available to all assesses irrespective of their status, including residential status. Accordingly, even non-resident investors such as FIIs would also enjoy the tax exemption.



Further, short-term capital gains arising on sale of securities in a recognized stock exchange in India, where such sale is effected on or after the notified date, will be taxed at the concessional rate of 10% under the new section 111A proposed to be inserted.

The proposed measures are likely to provide impetus to investments in Indian stock markets. However, owing to the transaction cost faced by the day traders and arbitrageurs, the levy of securities transaction tax may adversely impact the volumes of stock market transactions thereby affecting the general market sentiments and liquidity.

b) *Tax rebate under section 88D:*

A new section 88 D is proposed to be inserted for granting 100% tax rebate in the case of a resident individual where the total income does not exceed Rs. 1,00,000/- (US \$ 2,273). However, such individuals will be required to submit the tax returns if the total income exceeds Rs. 50,000/- (US \$ 1,136). This measure would provide relief to a large number of small tax payers.

c) *Tax holiday to undertakings building and developing housing projects:*

Presently, section 80 IB(10) provides for a deduction in respect of profits derived by an undertaking (enterprise) building and developing housing projects subject to fulfillment of certain conditions. It is now proposed to make following changes in this regard:

- Firstly, the benefit will be available in respect of projects approved before 31-03-2007 instead of the existing condition where a project is to be approved before 31-03-2005.
- Secondly, the projects must be completed within 4 years from the end of the financial year in which the housing project is approved by the local authority. At present no such condition exists.
- Thirdly, it is now clarified that the housing projects may include to some extent construction of shops and commercial establishments limited to 5% of the aggregate built up area of the project or 2000 sq feet, whichever is less. The existing provision lacks this clarity regarding construction of shops and other commercial establishments.
- Fourthly, and more significantly, the condition of the plot size of minimum one acre is proposed to be relaxed in case of a housing project carried out in accordance with a scheme framed by the Central Government or a State Government for reconstruction or redevelopment of existing buildings if such scheme is notified by the CBDT in this behalf. This measure would provide significant impetus for redeveloping/reconstruction of a large number of old and dilapidated buildings in cities like Mumbai.



d) ***Tax holiday to undertakings engaged in the business of processing, preservation and packaging of fruits and vegetables:***

Section 80 IB(11A) provides tax holiday to certain integrated business of handling, storage and transportation of food grains. It is now proposed to extend this benefit to the business of processing, preservation and packaging of fruits and vegetables. The tax holiday consists of 100% deduction for the profits derived from such business for the first five assessment years, and thereafter at 25% (30% in case of company) for the next five years. This incentive provision would substantially motivate development of the agricultural distribution system and fruit/vegetable processing and packaging industry.

e) ***Tax holiday for hospitals set up in rural areas:***

A new sub-section (11B) is proposed to be inserted in section 80 IB for granting 100% tax holiday for profits derived from the business of operating and maintaining hospitals in rural areas for the first 5 years, subject to the following conditions:

- Such hospital is constructed after 30th September, 2004 and before 1st April, 2008. For this purpose, the date of issue of completion certificate issued by the concerned local authority in respect of construction of hospital shall be deemed to be the date of its construction.
- The hospital has at least 100 beds for patients.
- The construction of the hospital is in accordance with the regulations of the local authority, and
- The assessee furnishes an audit report along with the return of income.

If one considers the definition of “rural area” as provided in section 80IB(14)(f), it would appear that in order to claim this benefit, one has to set up the hospital in an area having population of less than 10,000. The question, therefore, would be whether such a hospital of minimum capacity of 100 beds would be commercially feasible in such an area.

f) ***Tax holiday for substantial renovation and modernization of power transmission and distribution lines:***

At present, under section 80 IA 100% deduction is allowed in respect of profits derived from the business of generation of power or transmission or distribution of such power for a period of 10 consecutive assessment years out of 15 years beginning from the year in which such activity begins. It is now proposed to extend this benefit to an assessee who undertakes substantial renovation and modernization of the existing network of transmission or distribution lines at any time during the period 1st April, 2004 to 31st March, 2006. For this purpose, “substantial renovation and modernization” means an increase in the plant and machinery in the network of transmission and distribution lines by at least 50% of the book value of such plant and machinery as on 1st April, 2004.



g) Condition for additional depreciation under section 32(1)(iia) relaxed:

Under the existing provisions, an assessee gets additional depreciation @15% of the actual cost of new plant and machinery acquired and installed in an industrial undertaking after 31st March, 2002 for the purpose of substantial expansion of such undertaking if it was existing before 1st April, 2002. For this purpose substantial expansion would mean increase in installed capacity by not less than 25%. Now it is proposed to construe substantial expansion where the increase is 10% and above.

h) Tonnage tax scheme introduced for shipping companies:

A long awaited demand of shipping industry for changing the base of taxation of its business profits to a tonnage based presumptive taxation system, in line with the international practice has finally been accepted by the government. For this purpose, a new "tonnage tax" scheme has been proposed in Chapter XII – G of the Income-tax Act, 1961 comprising of sections 115V to section 115VZC. Broadly, under this scheme a qualifying shipping company is provided with an option to elect either the presumptive tonnage tax scheme or the normal provisions of the section 28 to 43C. Where the tonnage scheme is opted, the business profits of the shipping company from the business of operating qualifying ships and other incidental activities will be computed in accordance with the provisions of section 115VG (2) and (3). Sub-section (3) of section 115VG provides the presumptive rates of income per day in relation to the net tonnage of a qualifying ship, which are as under:

Qualifying ship having net tonnage	Amount of daily tonnage income
Upto 1,000	Rs. 46 for each 100 tons
Exceeding 1,000 but not more than 10,000	Rs. 460 plus Rs. 35 for each 100 tons exceeding 1,000 tons
Exceeding 10,000 but not more than 25,000	Rs. 3,610 plus Rs. 28 for each 100 tons exceeding 10,000 tons
Exceeding 25,000	Rs. 7,810 plus Rs. 19 for each 100 tons exceeding 25,000 tons

The daily income referred to above is to be multiplied by the number of days in the accounting year, and where the qualifying ship is operated only for part of the accounting year, then, by such number of days for which the ship is operated by the company. The income thus computed is deemed to be the business income of the shipping company. The other business incomes are to be computed under the normal provisions of the Act. The option once exercised generally runs for 10 assessment years unless the company, under certain circumstances disqualifies itself or opts out of the scheme. Elaborate provisions covering various conditions subject to which the scheme is made available, allocation of common cost, calculation of net tonnage, etc. are made under this Chapter. Thus, the new Chapter is a somewhat self contained code concerning the tonnage tax.



i) *Exemption for capital gains from certain agricultural land compulsorily acquired:*

Agricultural land is generally excluded from the definition of a capital asset under section 2 (14), unless it is situated within the jurisdiction of certain municipal corporation or a notified area within the prescribed limit upto 8 kms from such municipal corporation, etc. Therefore, generally, transfer of agricultural land, other than that referred to above, does not result in any taxable capital gain. However, transfer, whether by way of compulsory acquisition or otherwise, of agricultural land falling within the municipality or extended notified area referred to above give rise to capital gains. Perhaps with a view to enable infrastructure projects, and assist weaker agricultural land owners who are disrupted, it is now proposed to insert clause (37) in section 10 whereby an individual or HUF can claim exemption in respect of capital gain arising from transfer of agricultural land referred to above, if:

- the transfer is by way of compulsory acquisition under any law or the consideration for the transfer is determined or approved by the Central Government or the RBI.
- such land is used for agricultural purposes by such HUF or individual or his parent, during the period of two years immediately preceding the date of transfer, and
- the compensation or the consideration for such transfer is received after 31st March, 2004.

3.3 ADDITIONAL TAX BURDEN

a) *Gift received to be taxed as income:*

Levy of Gift tax was abolished in 1998. It is now proposed to revive the levy of Gift tax in a different manner by imposing income tax on the donees. To that effect, the definition of "income" in section 2(24) is sought to be enlarged to include any sum received by an individual or HUF from any person after 31st August, 2004, barring certain specified exceptions. Correspondingly, section 56 is also sought to be amended to include the aforesaid sum as income from other sources.

Broadly, any gift received from close relatives specified in the Explanation to section 2(24)(xiii), receipts under a will or by way of inheritance or in contemplation of death, receipts which are in the nature of income exempt under section 10 or any other section, receipts from employer and receipts on account of transfers of certain capital assets referred to under section 47 are excluded from the purview of the charge.



Further, an exemption u/s 10 (39) has been provided upto Rs.25,000/- (US \$ 568). Gifts received on the occasion of marriage are also exempted upto Rs. 1,00,000/- (US \$ 2,273) as explained in the notes on clauses.

It appears that the provision has been brought in as a measure to check tax evasion rather than as a revenue generating measure.

b) ***Exemption in respect of certain income of non-resident withdrawn:***

It is proposed to withdraw tax exemption hitherto available in relation to interest earned by a non-resident on NRE account. Accordingly, interest earned after 31st August, 2004 will attract tax. Similar provisions are also proposed in relation to interest payable after 31st August, 2004 by a scheduled bank to a non-resident or not ordinarily resident on deposit in foreign currency accepted by the bank as approved by the RBI.

c) ***Exemption in respect of Infrastructure Capital Company diluted:***

Under section 10 (23G), an infrastructure capital company enjoys tax exemption in respect of income by way of dividends (other than those referred to in section 115-O), interest and long term capital gains. It is now proposed that such income will be considered in computing the book profit and income tax payable under section 115JB. A corresponding amendment is also proposed in section 115JB to include this income within the ambit of book profit. Thus, the tax exemption currently enjoyed by an infrastructure capital company will be diluted to the extent of tax payable under section 115JB.

d) ***Denial of deduction for default in TDS:***

It is proposed to disallow business expenditure incurred by an assessee by way of interest, commission or brokerage, fees for professional services or fees for technical services, or payment to contractor/sub-contractor for which the amount is payable to a resident, if the assessee commits any default in compliance of provisions relating to tax deduction at source. However, where the tax is deducted or paid in any subsequent assessment year, the corresponding expenditure would be allowed in computing the income of that year in which such tax has been paid. However, a question arises as to what happens if tax is deducted and / or paid belatedly within the same accounting year. This may cause unintended hardship and give rise to avoidable tax litigation. It is, therefore, expected that necessary clarification is provided or the provision suitably amended at the stage of passing of the Finance Bill.



e) ***Prohibition for set off of business loss against salary income:***

Under section 71 inter-head set off is allowed, barring losses under the head capital gains and speculation loss. It is now proposed that where a loss is incurred under the head “Profits and gains of business and profession”, such loss will not be allowed to be set off against the income assessable under the head “Salaries”.

f) ***Amendment in section 90:***

Finance Act, 2001 had inserted an Explanation in section 90 with retrospective effect from 1st April, 1962 to provide that charging a foreign company at a rate of tax higher than that applicable to a domestic company shall not be regarded as a discrimination against such a foreign company where it has not made the prescribed arrangements for declaration and payments within India of the dividends payable out of its Indian income. In a recent ruling given by the Tribunal, this Explanation was held to be not applicable unless the rules are framed by the Board for declaration and payment of such dividends by the foreign company in India. Accordingly, it was ruled that the levy of tax at a higher rate was discriminatory against such foreign company. In order to overrule this decision, it is now proposed to amend the above explanation deleting the requirement of dividend declaration. Thus, a foreign company now cannot take this argument as was accepted by the Tribunal. However, a moot question remains as to whether a provision in the domestic law can deny a benefit provided in a tax treaty negotiated between two countries, where the well-settled law is that the provisions of tax treaties prevail over the domestic law.

g) ***Denial of loss on sale of units of mutual funds in certain cases:***

It is a common practice in the mutual fund industry to issue bonus units instead of dividend to attract investors. Typically, such investors dispose of their original holdings at reduced post bonus NAV and incur capital loss, though in substance, no such loss is effectively made. This route is adopted to avoid tax by both, the mutual fund as well as the investors. The mutual fund saves dividend distribution tax and the investors claims short term capital loss. Earlier, the law was amended to check dividend stripping transactions including those in the case of units of a mutual fund. However, a transaction structured by way of issue of bonus units was not covered. It is now proposed to plug this loophole.

As per the proposed provision, where a person buys or acquires any units of a mutual fund within a period of three months before the record date fixed for entitlement of bonus unit and sells or transfers within a period of nine months after such record date, either the original units or the bonus units or a combination thereof, then, the loss, if any, arising to him on account of the transaction of purchase and sale, will be ignored for the purpose of computing his taxable income. However, such loss will be deemed to be the cost of purchase of the bonus units.



h) *Dividend distribution tax payable by mutual funds increased:*

Under section 115R, a mutual fund pays dividend distribution tax at the rate of 12.5% on the amount of income distributed to its unit holders. It is now proposed with immediate effect (w.e.f 9th July, 2004) that dividend distribution tax will be levied at the rate of 20% on the income distributed to any person other than individual or HUF. In the case of individual and HUF unit holders, the tax rate continues to be 12.5%.

The income distributed by open-ended equity oriented funds up to 31st March, 2004 was outside the ambit of the tax imposed under section 115R. It is now proposed to extend this benefit to such open ended equity funds without a sunset clause.

3.4 CHANGES IN TAX PROCEDURES:

a) *Commissioner empowered to cancel registration of charitable trust /institution:*

Section 12AA provides the procedures for registration of a trust/institution by Commissioner of Income Tax. It is now proposed to insert a new sub-section (3) in section 12AA to empower the Commissioner to pass an order in writing cancelling the registration granted, if he is satisfied that the activities of such trust / institution are not genuine or are not being carried out in accordance with the objects of the trust / institution. However, before passing such an order it is necessary to give a reasonable opportunity of being heard to the concerned trust / institution.

b) *Assessing Officer to make reference to Valuation Officer for the purpose of section 69, 69A or 69B:*

It is proposed to insert new section 142A to provide that where an estimate of the value of any investment or any bullion, jewellery etc. is required to be made for the purpose of making any assessment or reassessment, the Assessing Officer may make a reference to the Valuation Officer to estimate such value and report the same to him. Once a reference is made to the Valuation Officer u/s. 142A, he shall have all the powers that he has under section 38A of the Wealth-tax Act, 1957. Upon receipt of the report from the Valuation Officer and after giving the assessee an opportunity of being heard, the Assessing Officer may take into account such report while finalizing such assessment or reassessment. This provision is proposed with retrospective effect from 15th November, 1972. However, the same shall not apply in respect of an assessment made on or before 30th September, 2004, and where such assessment has become final and conclusive on or before that date, except in cases where reassessment is required to be made under section 153A consequent to a search. It appears that this provisions has been proposed to negate the argument raised on behalf of the assesseees that the reference to Valuation Officer under the Income-tax Act could be made under section 55A only and not for the purpose of making addition u/s. 69, 69A or 69B.



c) *Limitation period for assessment extended where application is made to the Authority for Advance Ruling:*

It is proposed that where an assessee makes an application under section 245Q to the Authority for Advance Ruling, the time taken by the authority for disposing of this application is to be excluded for the purpose of computing the period of limitation prescribed for passing the assessment order.

d) *Amendment to Section 194 C:*

Under the existing provisions of section 194C, no tax is required to be deducted at source from any sum credited or paid in pursuance of any contract, the consideration for which does not exceed Rs. 20,000/- (US \$ 455). Thus, the key to apply this provision was the individual contract in pursuance of which the amount is credited or paid. Thus, in a given situation where the aggregate of sums paid during a financial year pursuant to two or more contracts exceed Rs. 20,000/-, no tax was required to be deducted where the consideration was less than Rs. 20,000/- with reference to the individual contracts. It is now proposed that where the amount of any sum credited or paid or likely to be credited or paid to the account of, or to, the contractor or sub-contractor exceeds Rs. 20,000/-, the tax would be required to be deducted at source. Further, where the aggregate of the amounts credited or paid or likely to be credited or paid during the financial year exceeds Rs. 50,000/- (US \$ 1,136), the person responsible for paying such sum shall be liable to deduct tax at source.

e) *Furnishing of Annual Information Return:*

The existing provisions of section 285BA provide that any assessee, who enters into any financial transaction, as may be prescribed, with any other person, shall furnish, within the prescribed time, an annual information return in such form and manner, as may be prescribed, in respect of such financial transaction entered into by him during any previous year. It is now proposed to enlarge the scope of reporting the prescribed transactions to the income-tax department. Besides the assessee, the onus is now also cast on other persons, such as a prescribed person in the office of Government, local authority or other public bodies, the Registrar or Sub-Registrar appointed under the Registration Act, 1908, registering authorities under Motor Vehicles Act, 1988, the Post Master General under the Indian Post Office Act, 1898, the Collector referred to in Land Acquisition Act, 1894, the recognized stock exchange under Securities Contracts (Regulation) Act, 1956, an officer of the Reserve Bank of India and the depository under the Depositories Act, 1996 to furnish annual information return in respect of the specified financial transactions.



④ **INDIRECT TAX PROPOSALS**

4.1 CUSTOM DUTIES

1. Peak rate of custom duty remained unchanged at 20%
2. Custom duty has been reduced from 20% to 15% on ferro alloys, stainless steel and other alloy steel(excluding seconds and defectives), copper, lead, zinc, tungsten magnesium, cobalt, cadmium, titanium and other base metals.
3. Custom duty has also been reduced from 16% to 10% on all primary, semi-finished and finished forms of iron and steel like ingots and billets, sponge iron, hot rolled and cold rolled bars/rod/coils of non-alloy steel.
4. Custom duty has been reduced from 20% to 15% on graphite, asbestos, mica fluorspar and felspar, gypsum.
5. Refractory and refractory inputs like graphite power, aluminous cement, calcined alumina, baron carbide, reactive alumina, silicon metal, micro/fumed silica, brown fused alumina, fused zirconia, silicon carbide, sodium hexameta phosphate, phenolic resin and fused silica to attract 15% custom duty instead of 20%.
6. Custom duty starches, palm oil increased.
7. Rehabilitation aids, phonographs, instruments and implants for the treatment/usage physically handicapped is exempt from custom duty.
8. Raw-material imported for manufacture of mobile phones also exempt from duties.

4.2 CENTRAL EXCISE:

1. Excise duty has been increased from 8 % to 16 % on following items with cenvat benefit.
2. Cakes and pastries, plastic insulated ware, vacuum flasks, scented supari, pre-fabricated buildings, laboratory glassware, clocks and watches of RSP not exceeding Rs. 500 (US \$ 11) per piece, monochrome television receivers, populated printed circuit boards for monochrome television receivers, imitation jewelry and candles. However, SSI exemption would be available to all these items.
3. The RSP limit for duty exemption raised from Rs. 125 (US \$ 3) to Rs. 250 (US \$ 6) per pair.



4. The excise duty reduced from 16% to 8% on gas stoves of RSP not exceeding Rs. 2000 (US \$ 45) per unit.
5. The value limit for pens and refills of ball pens as been raised from Rs. 100 (US \$ 2) to Rs. 200 (US \$ 5) per piece. Further, parts of pens and parts of refills have been exempted from duty.
6. Computers have been exempted from excise duty. Stand alone central processing units will also be eligible for the exemption. Parts captively consumed in the factory of the manufacture of computers also been exempted from excise duty.
7. Excise duty on non-alcoholic beverages, such as chocolates and malted food drinks, prepared and dispensed through vending machines has been exempted.
8. Tractors and captively consumed parts also exempted from the excise duty.
9. Milking machine and diary machine is also exempt from duty.
10. Excise duty on branded and packed preparation of meat, fish and poultry has been reduced from 16% to 8%.
11. Excise duty on food grade hexane has been reduced from 32% to 16%
12. Hand tools have been exempted from excise duty
13. Specified plantation machineries has been exempted from excise duty upto 30th April, 2005.
14. Cenvat scheme made optional to textiles and duties on textiles rationalised.
15. The equipment for hearing impaired, is exempt from excise duty.

4.3 SERVICE TAX:

Credit for service tax and excise duty is being extended across goods and services. The rate of service tax is proposed to be raised from 8% to 10%.

The following additional services are being covered in the net of service tax:

1. Business exhibition services
2. Airport services
3. Transport of goods by road by a goods transport agency
4. Transport of goods by air
5. Survey and exploration of minerals



6. Opinion poll services.
7. Intellectual property services other than copyrights
8. Forward contract services
9. Pandal or shamiana service
10. Outdoor catering
11. TV or radio programme production
12. Construction services in respect of commercial or industrial buildings or civil structures excluding construction road, bridges, dams, tunnel, railways, airport, long distance pipe line and transport terminal
13. Travel agents (other than air/rail travel agents)

It is clarified that the service tax is being restricted to the risk cover in life insurance service.

Scope of certain existing services is being extended as follows:

- * Commission and installation of plant, machinery or equipment to include “erection” thereof.
- * Stock brokers to include sub-brokers.
- * Cable operator service to include Multi System Operators.
- * Business auxiliary service also to include service relating to procurement of inputs, production of goods or provision of services on behalf of client. However, activities amounting to manufacture are specially excluded from the scope of service tax.
- * Financial services also to include other specified financial services, namely, lending, issue of pay order, demand draft, cheque letter of credit, bill of exchange, providing a bank guarantee, overdraft facility, bill discounting, safe deposit, lockers, or safe vaults and operation of bank accounts. The interest amount would, however, remain excluded from purview of service tax. In addition to banking company, financial institutions including a non-banking financing company, body corporate, any other commercial concern providing financial services will also be covered.
- * Tour operator services will include such package tour operators also who organize tours involving any mode of transport.

The following service tax exemptions are being removed:

- * Exemption to services in relation to safe deposit lockets and vaults
- * Maintenance or repairs of computers under a maintenance contract or by the manufacturer
- * Mandap keeper services provided by hotels. However, 40% abatement will be allowed if catering is also provided.



- * Commission agents, other than those dealing in agricultural produce, under business auxiliary service.
- * Broadcasting service provided by cable operators.
- * Reduction of abatement from 90% to 60% for non-package tours.

Exemptions given:

- * 40% abatement in convention service when catering is also provided.
- * 60% abatement to rent-a-cab scheme operators.

Major changes in Rules:

- * Mandatory penalty for non-registration is being removed
- * The present rate of interest of 15% on delayed payment of service tax is being replaced by a range, from 10% to 36% per annum. The Central Government will have the power to notify the rate of interest on delayed payment service tax within this range.
- * If the charges levied are inclusive of service tax then the service tax is required to be paid on gross amount charged or received.
- * If the input service supplier has not paid the service tax, the service tax credit cannot be recovered from the person availing the credit if he had taken reasonable steps in terms of Rule 5

4.4 SECURITIES TRANSACTION TAX :

Consequent to the proposal to abolish long term capital gain tax on listed securities, it is now proposed to impose a new transaction based tax called "Securities Transaction Tax". The tax will be levied at 0.15% of the value of taxable securities transaction entered into in any recognized stock exchange in India and is proposed to be collected from the buyer of the security. An obligation has been cast on the stock exchange to collect such tax from every buyer who enters into such a transaction.

The value of taxable securities transaction is to be computed with reference to:

- * the aggregate of the strike price and the option premium in the case of transactions relating to "options in securities";
- * the price at which "futures" is traded in the case of transactions relating to "futures"; and
- * the price at which securities are purchased in case of other securities transactions.



It appears that the tax will be imposed with reference to all securities transactions, whether it is delivery-based or not. It is expected that the volume of transactions especially those of speculators and arbitrage transactions will be reduced on account of this levy. Another interesting feature is that the tax is to be collected from the purchaser though the capital gain tax exemption is allowed to the seller. Further, since this turnover tax is not related to income, in a tax treaty situation, the same will not be covered under a tax treaty. Accordingly, claiming credit for the same in the foreign country (country of residence) seems almost impossible though one may possibly argue that having regard to the fact that logically this tax is imposed instead of capital gains tax and, therefore, in terms of economic substance it is in the nature of income tax only.

⑤ **OTHER MAJOR CHANGES**

- ❖ Sectoral cap on Foreign Direct Investments is proposed to be raised as under:
 - ✓ in Civil Aviation sector from 40% to 49%
 - ✓ in Insurance sector from 26% to 49%
 - ✓ in Telecom sector from 49% to 74%
- ❖ Procedure for registration and operation of FIIs is proposed to be made simpler and quicker.
- ❖ Investment ceiling for FII in debts funds is proposed to be increased from USD 1 billion to USD 1.75 billion.
- ❖ It is proposed to create an alternative trading platform for small and medium enterprises to raise equity and debt from the capital markets.
- ❖ It is proposed to set up an Investment Commission having broad authority of the Government to engage, discuss with, and invite, domestic and foreign businesses to invest in India. The Commission will woo domestic and foreign investors.
- ❖ It is proposed to bring out a scheme for realization of undisputed tax arrears. However, the details are yet to be announced.
- ❖ It is proposed to set up a Board for Reconstruction of Public Sector Enterprises to advise the Government on restructuring of PSEs, including disinvestment, closure or sale thereof.

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