

Post-Budget Memorandum - 2005

Executive Summary

Direct Taxes

The suggestions of the ICAI on the specified clauses of the Finance Bill, 2005, are given below briefly. Detailed reasoning follows thereafter. (Serial numbers refer to the corresponding numbers in the detailed suggestions)

1. Rates of tax
The proposed tax rates structure may be modified so that the benefit presently available to senior citizens and women tax payers below 65 years continues to be available.
2. Withdrawal of standard deduction in respect of income from salaries – Clause 6
The standard deduction under section 16 should be continued.
3. Amendment of the provision relating to amortisation of expenditure incurred under voluntary retirement scheme (Section 35DDA) – Clause 11
To avoid an ambiguous position that the exemption would be allowed only in respect of the amount, which the employee is to receive immediately on his retirement and not in respect of subsequent payments, the words “in connection with his voluntary retirement” may be substituted for the words “on his voluntary retirement”
4. Reduction in the rates of depreciation across the board for all assets and for all taxpayers – Paras 163 and 166 of the Budget Speech – Amendment in Appendix I to the Income-tax Rules, 1962 vide Notification No.67/2005, dated 28.2.2005.
The earlier rates of depreciation on general plant and machinery and other assets may be restored.
5. Trading in derivatives not to be deemed as speculative transaction – Clause 14 – Section 43
 - (a) Transactions other than those of derivatives carried out in a recognized stock exchange should not also be considered as speculative transactions. The distinction needs to be removed for all transactions carried out in a recognized stock exchange.
 - (b) It may be clarified that loss in share dealings carried out in a recognized stock exchange can be set-off against profits arising out of dealings in derivatives carried out in a recognized stock exchange.
6. Reduction in time limit for carry forward loss – Section 73 - Clause 20

A clarification may be made so as to enable the assessee to carry forward his speculative loss up to assessment year 2005-06 as per the old provision. Alternatively, the unadjusted speculative loss up to assessment year 2005-06 may be allowed to be carried forward for 4 assessment years from assessment year 2006-07.

7. New Section 80C – Clause 21
 - (a) PPF Rules should be amended to increase the limit of deposit to Rs.1 lakh.
 - (b) The condition that the qualifying investments for the purpose of section 80C should be made out of income chargeable to tax may be omitted.
8. Income-tax on fringe benefits – Chapter XII-H – Clause 37

In order to simplify the levy of fringe benefit tax and reduce litigation, the following suggestions are made for the consideration of the Government.

- (i) The existing Rule 3 of the Income-tax Rules should be retained and made stringent, so that perquisites and benefits which are enjoyed by employees individually are taxed in their hands as hitherto. This procedure is well tested for years and need not be disturbed.
- (ii) In any event, if the Government decides to consider individual heads of expenses as listed in the proposed section 115WB, the expenditure under the heads which are incurred for the employees should only be considered and the element of fringe benefit should not exceed 10% of the expenditure for levy of this tax. To take an example if labour welfare expenses are incurred, only 10% of such expenses should be considered as fringe benefits and the balance as business expenses. Here, it may be stated that Staff and Workers canteen expenses should be excluded from section 115 WB(2) as para 160 of the Budget speech states that such expenses will be excluded from fringe benefits. Even in this situation, traveling expenses for personal purposes, scholarships to children, use of employer's car etc. should be considered as perquisite in the hands of employees and taxed in their hands. So far as traveling, advertising, sales promotion and publicity are concerned, there cannot be any element of fringe benefits to employees and there-

fore such expenses should be excluded from section 115 WB(2). Further, if any expenditure is disallowed in the Income tax assessments as personal expenses (e.g. 25% of motor car expenses in the case of firm) the same should be excluded for computing fringe benefit tax.

- (iii) In the case of persons who are engaged in small businesses or professions, it would not be equitable to levy such a tax because no significant fringe benefits are provided to employees by such employers. Therefore, exemption from this tax can be granted where the turnover/gross receipts are less than Rs.50 lakhs and where the employees do not exceed 20.
 - (iv) Medical facilities which are not considered as a perquisite in terms of the proviso to section 17(2) should not be the subject matter of fringe benefit tax.
 - (v) Relief may be given from fringe benefit tax to genuine charitable institutions who are not carrying on business.
 - (vi) In section 115WJ relevant to advance tax on fringe benefits, it appears that though surcharge and cess are payable on an yearly basis, for the purpose of calculation of advance tax, only 30% of the value of fringe benefit is payable on a quarterly basis. This anomaly needs to be corrected.
 - (vii) In sub-section (3) of section 115WB, exclusion is provided for “perquisites in respect of which tax is paid or payable by the employees under Chapter IV.” Reference may be provided to perquisites as referred to in section 17(2)
 - (viii) Sections 115WB(2)(C) and 115WB(2)(E) may be amended to bring the provisions in line with clause (iii) and clause (iv) of sub-rule 7 of rule 3 for valuation of perquisites.
9. Amendment of section 139(1) first proviso – Clause 40(a)(iii)(C)
- (a) The words “during the previous year” may be inserted after the word “incurred”.
 - (b) Educational institutions, hospitals and mutual funds specified in the detailed suggestion may be required to file the return of income.
10. Banking cash transaction tax – Insertion of new Chapter VII
- (a) The proposal may be withdrawn. The government may notify that all banks would be required to submit the required information in the Annual Information Return. Further, all taxpayers may be required to give details of all

their bank accounts in their return of income.

(b) If the above suggestion is not acceptable, the following suggestions may be taken into consideration

- (i) the limit of Rs.10,000/- may be increased to 50,000/-. From the administrative view it will be easier.
- (ii) Further, the limit per day should be with reference to each branch of a bank and not with reference to each bank. It will be difficult for each bank to monitor transactions in different branches and decide about collection of tax by aggregating withdrawals by a person from various branches on a single day. A company having several branches and having accounts in various branches of the same bank may withdraw smaller amounts in cash. To aggregate all these withdrawals on a single day and collect tax if the aggregate exceeds the above limit will be an impossible task for the bank.
- (iii) Remittance of cash by a branch of a bank to branch of another bank to facilitate payment to customers should be excluded from the levy of this tax.
- (iv) If at all the levy is to be retained in the statute, the limit should be realistic and linked to the turnover or total expenditure (both capital and revenue). In that case the Government need not cast the responsibility on the banks to collect the special tax. The assessee may be asked to furnish relevant information in the return of income and form of return may be suitably redesigned. Form 3CD for tax audit report may also be suitably amended so that the tax auditor can certify the amount of cash withdrawal.
- (v) Further, under the proposed provisions, those who are in business or profession can claim deduction of banking cash transaction tax in the computation of income from business or profession. However, the assessee having no business or profession cannot avail the benefit of such deduction.

Service Tax

The suggestions of the ICAI on the specified clauses of the Finance Bill, 2005 relating to service tax and also the relevant rules are given below briefly. Detailed reasoning follows thereafter. (Serial numbers refer to the corresponding numbers in the detailed suggestions)

A. SUGGESTION FOR CHANGES IN THE FINANCE BILL, 2005

1. Import of services – issues to be addressed – Place of Supply Rules to be introduced
 - (a) The proposed Explanation may be deleted from section 65 and a new section may be drafted so as to empower the Government to draft Rules for determining the place where services shall be deemed to have been provided, known as the ‘Place of Supply Rules’ which shall be applicable to both import and export.
 - (b) The Export of Services Rules, 2005 maybe consolidated into a new set of rules known as ‘Place of Supply Rules’ which would determine the ‘place where services are provided’ and therefore deal with both import and export of services. The ‘Place of supply Rules’ is present in all the nations where there is a tax on services e.g. United Kingdom, Ireland, etc.
2. Taxable service to include ‘service to be provided’ – proposed amendment maybe deleted.
The present provisions namely “service tax should be applicable on services provided” should continue. The situs of taxation should be services provided but, the payment of tax may be made when the amount is collected. Hence it is hereby suggested that the words “or to be provided” in section 65(105) be deleted. Consequential amendments made in section 67 and the proposed new explanation 2 to section 67 may also be deleted. Further the erstwhile Explanation in rule 6(1) clarifying the method of calculation of service tax for payments received in advance should be reinstated.

B. SUGGESTIONS FOR CHANGES IN THE EXPORT OF SERVICES RULES, 2005

3. Notifications granting rebates in relation to service exports to be issued immediately.
The notifications granting the rebates mentioned in the detailed suggestion may be issued expeditiously and may take effect from 15th March, 2005.
4. Certain concessions given in Circular No. 56/8/2003 dated 25.4.2003 to be specifically included in the Export Rules.
The Notifications granting rebates as mentioned in para 3 of the detailed suggestion must also provide for such a concession as mentioned in the Circular No. 56/8/2003 dated 25.4.2003.
5. Export where recipient of service located outside India - Condition of delivery of service outside

India may be dispensed with.

Export services being intangible cannot be delivered physically like goods which are tangible. Hence, the condition of delivery may be dispensed with. The condition that the service should be used in business outside India would meet with the requirements of exports.

6. Certain changes in the categorization of services – Mandap keeper services to fall under rule 3(1) instead of rule 3(2) and Practicing chartered accountants, cost accountants and company secretaries to fall under rule 3(3) instead of rule 3(2).
Mandap keeper services are services relating to immoveable property. Thus, the mandap keeper’s services must be included in rule 3(1) alongwith other services relating to immoveable property. Similarly, it is also suggested that services provided by Practicing Chartered Accountants, Practicing Cost Accountants and Practicing company Secretaries [clauses (s), (t) and (u) of sub-section (105) of section 65 respectively] being professional services must be categorized under rule 3(3) along with other professional services such as management consultants, consulting engineers, etc. according to which the services are considered as exported if recipient of the service is located outside India.

C. SUGGESTIONS FOR CHANGES IN THE SERVICE TAX RULES, 1994

7. Due dates of service tax to be kept at 15th of the following month / quarter instead of 5th and payment for the latter half of March maybe made by 15th April.

The due dates for payment of service tax (except March) may be postponed from 5th of the following month / quarter to 15th of the following month / quarter. Further, in case of payments for the month / quarter ending March the payment maybe made in two instalments as suggested in the table below.

The due dates could thus be summarized as under :

Status of payer	Period	Due date
Companies	All months except March	15 th of the following month
	1 st March – 15 th March	25 th March
	16 th March – 31 st March	15 th April
Other than Companies	All quarters except January – March	15 th of the month following the relevant quarter
	1 st January – 15 th March	25 th March
	16 th March – 31 st March	15 th April

8. Rule for issue of Invoice / bill / challan within 14 days from date of completion of service or receipt of payment whichever is earlier to be modified to -
- (i) make the time limit as 14 days from the end of the month in which service is completed
 - (ii) dispense with the requirement to issue an invoice for advance payments – instead a ‘receipt’ maybe issued

The condition of issue of an invoice on advance payments may be dispensed with. Instead the Rules could provide for issue of a ‘Receipt’ – a document for proof of receipt of money.

The rule may be modified to provide for issue of an invoice within 14 days from the end of the month in which service is completed.

9. Mutual fund / Asset Management Companies to pay service tax on mutual fund distribution services - clarifications

The relevant clause may kindly be redrafted in the manner suggested in the detailed suggestion.

IMMEDIATE ATTENTION.

10. Revision of returns
There should be a provision for revising the returns, which is absent in the present dispensation.
11. Clarifications / Changes in the CENVAT Credit Rules, 2004
There are certain clarifications / changes which may be considered in the area of CENVAT Credit Rules, 2004. These are as follows:
- (i) Clarification on the availability of input tax credit for service tax paid on reimbursable expenses or pass through transactions.
 - (ii) Refund of CENVAT credit to service providers.
 - (iii) Input credit on export services.
 - (iv) Obligation of manufacturer of dutiable and exempted goods and provider of taxable and exempted services – Rule 6 drafting improvements
 - (v) Clarification on availability of input tax credit if only part payment is made to the input service provider.
 - (vi) Transitional provision
 - (vii) Condition of receipt of capital goods in the premises of the output service provider. ■

D. MATTERS NOT CONSIDERED IN THE FINANCE BILL, 2005 BUT REQUIRING

ANNOUNCEMENT

Empanelment as a Peer Reviewer

As members are aware, Peer Review Mechanism put in place by the Institute, as per the Statement on Peer Review, has commenced with the implementation of stage I w.e.f. 1st April, 2003. The reviews are to be carried out by Reviewers empanelled with the Peer Review Board. The criteria for empanelment as a Reviewer is that a person should -

1. be a member;
2. possess at least fifteen years’ experience of audit; and
3. be currently active in the practice of accounting and auditing.

Applications were invited from members fulfilling the above criteria for empanelment with the Board. More than 2000 members have been empanelled as Reviewers. Applications received in the recent past are under process.

With the implementation of stage II w.e.f. 1st April, 2004, the number of Practice Units to be reviewed, selected on random sample selection, through a specially developed software, is substantial and from mofussil areas like Ambabari, Bareilly, Bhilwara, Bilaspur, Chittaurgarh, Gorakhpur, Lashkar, Muzaffarnagar, Panipat, Ameerpet, Anantapur, Belgaum, Eluru, Hubli, Nellore, Salem, Bid, Jalgaon, Miraj, Petlad, Solapur and Yavatmal. In addition, Practice Units under stage I have also

been selected for Phase II of stage I.

To ensure that the reviews are carried out in time and as many PUs are reviewed as possible, including those located at places mentioned above, the Board wishes to enlarge the resource pool of Reviewers. Members fulfilling the criteria mentioned above are invited to empanel themselves as Reviewers by applying in the prescribed format (available on Institute’s Website www.icai.org under the link ‘PEER REVIEW BOARD’ or can be obtained from the Institute’s Office at New Delhi) and send to Shri Vijay Kapur, Secretary, Peer Review Board, The Institute of Chartered Accountants of India, P.O. Box 7100, I.P. Marg, New Delhi 110 002.

We hope, in order to achieve the objective of Peer Review viz., enhancement in the quality of attestation services performed by the members of the Institute, cooperation would be forthcoming from the members by empanelling as a Reviewer.

Secretary,
Peer Review Board