

28 February 2011

Budget PLUS 2011 Tax Alert

Retail and Consumer Products Sector

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Foreword

Union Finance Minister presented the Union Budget for 2011 on 28 February 2011. The Budget was presented in the backdrop of the swift and broad based growth achieved in 2010-2011 along with GDP growth of 8.6% in 2010-2011 in real terms.

For the Retail and Consumer Products sector, various policy initiatives have been introduced to achieve efficiencies in the distribution and marketing systems of food grains, fruits, vegetables, poultry, expansion of agricultural credit, etc.

Further, Budget speech mentions that the areas of divergence with States on proposed Goods and Services Tax (GST) have been narrowed. As a step towards roll out of GST, Constitution Amendment Bill is proposed to be introduced in this session of Parliament

This Alert summarizes key policy reforms and key direct and indirect tax proposals impacting the Retail and Consumer Products sector.

FDI policy reforms

Economic Survey 2010-2011

- ▶ The Economic Survey for 2010-2011 has recommended allowing Foreign Direct Investment ('FDI') in multi-product/ multi-brand retail in a phased manner beginning with metros and to incentivize the existing retail shops to modernize.

Union Budget 2011-2012

- ▶ No announcements on permitting FDI in retail are made in the Budget.
- ▶ However, Budget speech mentions that discussions are underway to further liberalize the FDI policy.

Key direct tax proposals impacting Retail and Consumer Products sector

Personal income-tax

- ▶ Basic exemption limit applicable for individuals has been proposed to be increased to INR 180,000 from INR 160,000.
- ▶ Age threshold for senior citizens has been proposed to be revised to 60 years from 65 years. Further, basic exemption limit for senior citizens has been proposed to be raised to INR 250,000 from INR 240,000. Additionally, it has been proposed to increase the basic exemption limit for senior citizens aged 80 years or above to INR 500,000.

Corporate tax rates

- ▶ It is proposed to reduce the surcharge from existing 7.5% to 5% for domestic companies having a turnover of more than INR 10 million.

- ▶ Further, it has been proposed to reduce the surcharge from existing 2.5% to 2% for foreign companies having a turnover of more than INR 10 million.
- ▶ Thus, the effective tax rates for domestic companies shall reduce from 33.22% to 32.445%. Also, the effective tax rates for foreign companies shall reduce from 42.23% to 42.024%.

Minimum Alternate Tax ('MAT')

- ▶ The existing rate of MAT at 18% (plus surcharge and education cess) of book profits has been proposed to be marginally increased to 18.5% (plus surcharge and education cess).
- ▶ Further, MAT exemption available to SEZ developers and units has been proposed to be withdrawn.

Alternate Minimum Tax ('AMT')

- ▶ It has been proposed to levy AMT in respect of Limited Liability Partnerships ('LLP') at 18.5% (plus education cess) of adjusted total income (increased by Chapter VI-A deductions and deductions claimed in respect of profits of SEZ units) if regular income-tax on total income of LLP is less than the AMT.
- ▶ AMT credit, carry forward and set off - similar to provisions under MAT.

Foreign dividends

- ▶ Presently, dividend received by Indian parent companies from foreign subsidiaries is taxable in the hands of the Indian parent company at the maximum marginal rate of tax (ie 30% plus surcharge and cess).

- ▶ It has been proposed to tax the dividend declared, distributed or paid by a subsidiary foreign company at 15% on a gross basis.
- ▶ This amendment is proposed to take effect from 1 April 2012.

Other incentives

- ▶ Investment linked deduction in the form of 100% deduction of capital expenditure (other than on land, goodwill and financial instrument) also extended to new plant or newly installed capacity in an existing plant for production of fertilizer. This amendment is proposed to take effect from 1 April 2012.
- ▶ Weighted deduction enhanced from 175% to 200% for any sum paid to National Laboratory or university or Indian Institute of Technology engaged in approved scientific research programme. This amendment is proposed to take effect from 1 April 2012.

Transfer Pricing

- ▶ Due date for filing tax returns have been extended to 30 November in case of corporates filing transfer pricing certificates.
- ▶ Further, the benefit of +/-5% variation is proposed to be changed to a percentage to be notified by the Government.
- ▶ Additionally, the power provided to transfer pricing officers has been proposed to be expanded to include power to conduct survey and to consider international transactions not referred to them.

Reporting by Liaison Offices ('LOs')

- ▶ It has been proposed that LOs would need to file annual information statement, as may be prescribed, within 60 days from the end of financial year. This amendment is proposed to take effect from 1 June 2011.

Anti-avoidance measures

- ▶ In order to strengthen the system of collection of information from foreign tax jurisdictions it has been proposed to provide a toolbox of counter measures to discourage transactions with entities located in non-cooperative jurisdictions as may be notified by the government.
- ▶ Consequently, transfer pricing provisions would be applicable even for transactions with unrelated parties if located in such notified jurisdictions. Further, deductions may be restricted for specified transactions undertaken with entities in such jurisdictions. Any payments made to a person located in notified jurisdictional area shall be liable to tax deduction at higher of the specified rates or 30%. Receipts/credits from person in notified jurisdictional areas to be treated as deemed income of Indian taxpayer, if source of money in the hands of such person or the beneficial owner not explained satisfactorily

Key indirect tax proposals impacting Retail and Consumer Products sector

Customs duty

- ▶ Standard rate if customs duty maintained at 10%

Changes in basic customs duty rates

Product	Basic duty		Movement
	From (%)	To (%)	
Lactose used in the manufacture of homeopathic medicine	25	10	↓
Life saving drugs such as Rasburicase, Nilotinib, Pneumococcal sacchrude Conjugate Vaccine, etc	10	5	↓
Nylon chips, yarn and fibre	10	7.5	↓
Specified gems and jewellery machinery	7.5	5	↓

- ▶ Exemption on import of parts, components and accessories for manufacture of mobile handsets continued upto 31 March 2012.
- ▶ This will help in maintaining prices of mobile handsets manufactured in India with imported components and accessories.
- ▶ Assessment of customs duty will now be on 'Self assessment' basis. This is likely to reduce hassles associated with import of goods.
- ▶ Above changes are applicable from 1 March 2011.

Central Excise Duty

Changes in basic excise duty rates

Product	Basic duty		Movement
	From (%)	To (%)	
Microprocessor (other than motherboards), floppy disc drive, etc when meant for external use with a computer or laptop as a plug in device	NIL	5	↑
Notebooks and exercise books	NIL	1*	↑
Telephone sets and other transmission apparatus	NIL	1*	↑
a) Mobile handsets, radio trunking terminals b) Wireless data modems cards			
Storage devices	NIL	1*	↑
a) CDs, VCDs, DVDs b) Sound / video recorded magnetic tapes, cassettes, discs etc c) Smart cards			
Cost of branded jewellery and articles of gold, silver and precious metals	NIL	1*	↑
Sanitary napkins (falling under Chapter Heading 4818 40 90), baby and clinical diapers and adult diapers (falling under Chapter Heading 4818 40 10)	10	1*	↓

*subject to non availability of cenvat credit

- ▶ Standard rate of central excise duty has been maintained at 10%. However, the merit rate of excise duty (CENVAT) for non petroleum goods has been increased from 4% to 5%.
- ▶ On account of this amendment, products which are hitherto attracting basic excise duty of 4% would now attract 5%. The effective duty rate would, therefore, increase from 4.12% to 5.15%.

- ▶ Exemptions from excise duty on number of products have been withdrawn. In some cases where the tariff rate of those items which attracted NIL duty has been fixed at 5% ad valorem.
- ▶ A nominal duty of 1% ad valorem has been imposed inter alia on number of items with a condition that no credit of duty paid on input and input services is taken.
- ▶ Branded readymade garments and textile articles brought under the mandatory duty regime. General SSI scheme also extended to such goods.
- ▶ AED (GSI) amended to exclude sugar, textile and textile products from its purview. This will enable State Governments to levy VAT on such goods.

All of the above changes are applicable from 1 March 2011.

- ▶ Definition of 'inputs' under central excise has been revised. Henceforth, all goods used in the factory of manufacturer of the final product, except those specified in the negative list and goods having no relationship whatsoever with the manufacture of final product, would qualify for treatment as inputs.
- ▶ This would be effective from 1 April 2011

Service tax

- ▶ Standard rate if service tax maintained at 10%
- ▶ Trading activity has been specifically included in the definition of exempt services. This has set at rest whether trading should be considered as a service.

Given this, Cenvat credit attributing to gross margin on trading activity will require to be reversed.

- ▶ Rule 6(5) of the CCR providing for full Cenvat credit in respect of 16 specified input services omitted. This will lead to reduction in Cenvat credit available.
- ▶ Definition of input service has also been rationalized to impart clarity and achieve congruence with the definition of inputs. This would be effective from 1 April 2011
- ▶ The Point of Taxation Rules 2011 have been framed and made effective from 1 April 2011. These rules would determine the point in time when the services shall be deemed to be provided. The general rule will be that the time of provision of service will be the earliest of the of the following date:
 - ▶ Date on which service is provided or to be provided
 - ▶ Date of invoice
 - ▶ Date of payment

Central sales tax

- ▶ Rate of Central sales tax (against Form C), maintained at 2%.

Goods and service tax

- ▶ Constitutional amendment bill to introduce Goods and Service tax is proposed to be presented in this budget session.

Key Policy Initiatives impacting Retail and Consumer Products sector

Mega Food Parks

- ▶ 15 Mega Food Parks to be set-up under The Eleventh Plan to address the issues relating to bottlenecks in retailing capacity of vegetables and fruits.

Storage Capacity and Cold Chains

- ▶ The process of augmenting the storage capacity for food grains through private entrepreneurs and warehousing corporations proposed to be fast tracked.
- ▶ To attract investments in cold storage projects, capital investment in the creation of modern storage capacity to be made eligible for viability gap funding scheme of the Finance Ministry.
- ▶ Also, it has been proposed to recognize cold-chain and post-harvest storage as an infrastructure sub-sector.

Agricultural initiatives

- ▶ For better distribution of fruits, vegetables, milk, meat, poultry and fish, the total allocation to Rashtriya Krishi Vikas Yojana increased from INR 6,755 crore to INR 7,860 crore.
- ▶ Towards bringing Green Revolution to the eastern Region, INR 400 crore allocated to improve rice based cropping in eastern India.
- ▶ INR 300 crore allocated towards each of the following initiatives:
 - ▶ To bring 60,000 hectares under oil palm

plantations in an initiative to yield about 3 lakh metric tonnes of palm oil annually in five years.

- ▶ To implement vegetable initiative to provide quality vegetables at competitive prices.
- ▶ To promote animal based protein production through livestock development, dairy farming, piggery, goat rearing and fisheries.
- ▶ To promote higher production of Bajra, Jowar, Ragi and other millets.
- ▶ Need highlighted for the State Governments to review and enforce a reformed Agriculture Produce Marketing Act.
- ▶ In view of the National Mission for Sustainable Agriculture, it has been proposed to promote organic farming methods, combining modern technology with traditional farming practices.
- ▶ Capital investment in fertilizer production proposed to be included as an infrastructure sub-sector.

Mega cluster scheme

- ▶ Considering the large employment and export potential of Mega clusters, it has been proposed to extend the Mega Cluster Scheme for development of leather products.
- ▶ Further, seven mega leather clusters would be set up during the year 2011-12.

Unfinished agenda

- ▶ Going forward, the Retail and Consumer Product sector would await the accomplishment of unfinished agenda on developments around opening up of Retail sector to FDI and timely implementation of GST.

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