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Finance Bill 2011

Note on the provisions of Finance Bill - Part II

9th March 2011

1. MAT on LLP:

1.1 Limited Liability Partnership (LLP) law has been enacted about 2 years ago. LLP offers the benefit of a limited liability as in case of a company. At the same time it offers reduced compliance with the rules which are normally there for a company.

An LLP also has 2 distinct tax advantages. One is that any distribution from an LLP is not liable to Dividend Distribution Tax. Secondly, Minimum Alternative Tax (MAT) is not leviable. Several promoters have converted their holdings in listed companies from companies into LLPs.

The LLP will continue to be exempt from DDT. However MAT is now proposed to be levied as per the Finance Bill 2011.

1.2 The MAT has been proposed as **18.5%** - as in the case of companies. Surcharge will not be payable by an LLP, whereas a company is liable to surcharge. Education cess will be levied for an LLP just as in case of companies.

1.3 MAT is imposed @ 18.5% on adjusted income. Income-tax is on normal income computed as per Income-tax Act after claiming all deductions, etc. If Income-tax is less than MAT, assessee will be liable to pay MAT.

Adjusted income means taxable income as increased by deductions under chapter VI-A (infrastructure benefit, etc.) and income under section 10AA (SEZ units).

In essence, **deductions and SEZ reliefs cannot be used to reduce the taxes below 18.5%.**

1.4 If MAT is more than the normal tax, the excess is available as a credit against normal tax of subsequent years. The excess can be set off within a period of 10 years. This provision is similar to MAT for companies.

2. Liaison offices:

A liaison office normally cannot have any income. RBI does not permit liaison offices for income generating activities.

However some liaison offices do carry out business generating activities. In recent times, the tax officers have started taking action against such liaison offices. As no returns are filed by such liaison offices, the tax officers do not have any knowledge of their activities in India.

The finance bill now proposes that the liaison offices will have to file a statement (which will be prescribed later) within 60 days of the end of the financial year.

3. Capital expenditure deduction:

3.1 The Government is moving away from income based reliefs to investment based reliefs. For specified industries, deduction is available for capital investments in plant and machinery and other capital assets used in the specified businesses (except land, acquired goodwill or financial instruments).

The deduction is available for following businesses:

- (i) setting up and operating a cold chain facility;
- (ii) setting up and operating a warehousing facility for storage of agricultural produce;
- (iii) laying and operating a cross-country natural gas or crude or petroleum oil pipeline network;
- (iv) building and operating, anywhere in India, a new hotel of two-star or above category as classified by the Central Government;
- (v) building and operating, anywhere in India, a new hospital with at least one hundred beds for patients;
- (vi) developing and building a housing project under a scheme for slum redevelopment or rehabilitation.

The finance bill has proposed the relief for two more businesses:

- i) housing project for affordable housing.
- ii) new plant or newly installed capacity for fertiliser production.

Entire amount of investment in capital assets (except land, acquired goodwill or financial instruments) is allowed as a deduction. In essence it is an advance depreciation – by allowing the entire cost as a deduction.

- 3.2 The finance bill further clarifies that the loss from specified businesses can be set off against profits from specified businesses (even if the same have not availed of any benefit under section 35AD.) This is a welcome clarification.

4. **Deduction for payment for scientific research:**

For payment made for scientific research to any institution like National Laboratory, IIT, etc., a deduction of 175% of the payment is allowed. Thus for a payment of Rs. 1,00,000, a deduction of Rs. 1,75,000 is allowed. This limit is proposed to be increased to 200% of the payment made.

5. **Transfer Pricing audit:**

The due date for transfer pricing report is 30th September. The finance bill proposes to give more time for preparing the transfer pricing report as by 30th September, comparable data may not be available. Hence to give more time to conduct a transfer pricing analysis, it is proposed that the due date for transfer pricing will be 30th November.

However the date for tax audit continues to be 30th September!

6. **Power project:**

Infrastructure projects are granted tax exemptions. Power projects are considered as infrastructure projects and allowed tax exemptions. For the exemption, it is necessary that the power project should commence generation of power by 31st March 2011. This date has been extended by one more year – upto 31st March 2012.

7. **Charitable purpose:**

Trusts and companies are exempt from income-tax if they are formed for “charitable purpose”. The exemption is subject to the guidelines and rules under the Income-tax Act. “Charitable purpose” has been defined to include several activities like relief for the poor, education, etc.

One of the purposes is “advancement of any other object of general public utility” (**public utility**). **Public utility** includes any purpose like advancement of art, sports, commerce, etc. If the public utility activity involves any business, trade, etc., then it is not considered as “charitable purpose”. For example, a trade organisation is formed for studying trade activities in India. This is an activity of public utility. It conducts a seminar on

trade in India. For the seminar, it charges fees. This activity can become a business activity. (It is not necessary that there should be a profit, or an intention of making a profit.) This will normally mean that if the trade organisation earns even Re. 1, it would not be eligible for exemption.

Therefore an exemption is provided that in case receipt from a business activity is less than Rs. 10 lakhs in a year, it will not be considered as business activity. Thus small activities of organising conferences, etc. will not amount to trade.

The finance bill has proposed to increase the limit to Rs. 25 lakhs.

8. Investment in pension scheme:

A deduction is available for deposit in the New Pensions Scheme (NPS). The cumulative amount available for deduction is Rs. 1,00,000 for various investments – NSC, PPF, etc. At present, the employer's and employee's contribution is considered within the limit of Rs. 1,00,000. The finance bill proposes to consider only the employee's contribution within the limit of Rs. 1,00,000. This is a relief giving provision. This will bring the relief at par with other existing schemes like PPF and EPF.

Further, the employer will be eligible for a deduction for the contribution made to the NPS to the extent it does not exceed 10% of the salary.

9. Infrastructure bonds:

A deduction of Rs. 20,000 is available to an assessee for investment in infrastructure bonds. This deduction was available for investment upto 31st March 2011. The date has been extended upto 31st March 2012. There are several companies which have come out with Infrastructure bonds.

10. Tax on income distributed by Money Market Mutual Funds:

Under the existing provisions, dividends distributed by Money Market Mutual Funds (MMMFs) were taxed at a rate of 25 percent. This tax is paid by the MMMFs. During discussions with the tax revenue officials, it was learnt that the provision was aimed at encouraging investment by individuals. However, from their statistics, it was apparent that majority of the investment in such funds was being made by companies. This was because of the 5 percent arbitrage that these companies enjoyed. If they keep the money in the bank, the interest is taxed @ 30%. If the money is kept with MMMFs, the tax is 25%. On large amounts, even a small difference in the yield, makes a big difference in the income.

To bring the benefit in line with the intention, it is proposed to levy a 30 percent tax on incomes distributed by money market mutual funds to any person other than an individual or HUF.

11. Exemption from filing of tax returns for certain class of assesseees:

The Finance bill has proposed to relax the return filing requirements for specified classes of assesseees. The Memorandum explains that salaried tax payers whose entire tax liability is discharged by the employer through TDS would not be required to file tax returns. This is because the information is available with the tax department by way of reporting by employers through TDS statements already.

This relaxation would be subject to rules which are to be notified by the tax department.

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