PROJECT REPORT ON

A STUDY ON TAX & NON-TAX REVENUE IN INDIA

SUBMITTED BY

ASHISH S TIWARI

T.Y.B.M.S. SEMESTER –V

UNDER THE GUIDANCE OF

PROF. HITESH BIYANI

SUBMITTED TO

UNIVERSITY OF MUMBAI

THROUGH

SMT. KAMALADEVI GAURIDUTT MITTAL

COLLEGE OF ARTS & COMMERCE

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DECLARATION

I, **ASHISH S TIWARI** of **SMT. K.G MITTAL COLLEGE OF ARTS & COMMERCE** of T.Y.B.M.S (semester-v), hereby declare that I have completed the project on **A STUDY ON TAX & NON-TAX REVENUE IN INDIA** in the academic year 2014-2015.

The information submitted is true and original to the best of my knowledge.

Date: _____________

(ASHISH S TIWARI)

CERTIFICATE

This is to certify that, **Mr. ASHISH S TIWARI,** a student of T.Y.B.M.S. has successfully completed project on **A STUDY ON TAX & NON-TAX REVENUE IN INDIA** in the academic year 2014-15 under the guidance of **PROF. HITESH BIYANI**

HITESH BIYANI	**PROF NAMRATA ARORA**
(PROJECT GUIDE)	**(BMS CO-ORDINATOR)**

DR. SUHASINI ARYA	**EXTERNAL EXAMINER**
(COLLEGE PRINCIPAL)	

PROJECT GUIDE CERTIFICATE

I, **PROF. HITESH BIYANI** hereby certify that **Mr. ASHISH S TIWARI** of **SMT. K.G.MITTAL COLLEGE OF ARTS & COMMERCE** T.Y.B.M.S, (semester-v) has completed project on **A STUDY ON TAX & NON-TAX REVENUE IN INDIA** in the academic year 2014-2015.

The information submitted is true & original to the best of my knowledge.

Date:____________________

____

PROF. HITESH BIYANI

(PROJECT GUIDE)

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Date: _____________

(ASHISH S TIWARI)

A STUDY ON TAX &NON-TAX REVENUE IN INDIA

Index

Sr. No.	Topics	Page No.

	Executive Summary	
1	Introduction	1-2
2	History and objective of tax law	3-5
3	Types of Taxes and Non – Tax revenue	6-19
4	Professional Tax	20-25
5	Value Added Tax	26-40
6	Entertainment Tax in India	41-46
7	Advantage and Disadvantahe od Taxation to resdistribute Income	47-49
8	Case Study	50-57
9	Survey Finding	58-67
10	Conclusin	68
11	Bibliography	59

EXECUTIVE SUMMARY

Income tax is all income other tha agricultural income levied and collected by the central government and shared with the states. As per Income Tax Act 1961, every person, whose net income exceeds the exemption limit comes under the tax net and he shall be charged tax at the rate or rates prescribed in the finance atc. Such income tax shall be paid on the total income of

the previous year in the relevant assessment year. The total income of an individual is determined on the basis of his residential status in India.

There are two types of taxes in India- Direct tax and Indirect tax.

- In direct tax burden falls directly on the tax payer.
- In indirect tax the burden can be transferred to thr third party.

CHAPTER-1

INTRODUCTION

TAXATION SYSTEM IN INDIA

India has a well-developed tax structure with clearly demarcated authority between Central and State Governments and local bodies. Central Government levies taxes on income (except tax on agricultural income, which the State Governments can levy), customs duties, central excise and service tax.

Value Added Tax (VAT), (Sales tax in States where VAT is not yet in force), stamp duty, State Excise, land revenue and tax on professions are levied by the State Governments. Local bodies are empowered to levy tax on properties, octroi and for utilities like water supply, drainage etc. In last 10-15 years, Indian taxation system has undergone tremendous reforms. The tax rates have been rationalized and tax laws have been simplified resulting in better compliance, ease of tax payment and better enforcement. The process of rationalization of tax administration is ongoing in India.

Since April 01, 2005, most of the State Governments in India have replaced sales tax with VAT.

- Taxes Levied by Central Government • Direct Taxes
- Tax on Corporate Income
- Capital Gains Tax
- Personal Income Tax
- Tax Incentives
- Double Taxation Avoidance Treaty
- Indirect Taxes
- Excise Duty
- Customs Duty
- Service Tax
- Securities Transaction Tax
- Taxes Levied by State Governments and Local Bodies
- Sales Tax/VAT
- Other Taxes

OBJECTIVES OF THE STUDY:

- To study about the Collection of revenue which is collected by the government in the form of taxes & Non-taxes revenue
- To analysis how the collecting revenue redistributed for social welfare in form of public expenditure.
- The purpose of the study is to get detailed knowledge about taxation System in India.
- The purpose of the study is to help the tax Payer to briefly understand the need for charging Tax and the benefits out of that.

Methodology:

- The project consists of information collected from various sources like books, websites.
- This has at times supplemented by own interpretations.
- This information required for the completion of this comprehensive study has been taken from various websites and books the names of which have been mentioned in the bibliography.

CHAPTER-2

HISTORY AND OBJECTIVES OF TAX LAW

Meaning:

Tax Law in our country is as old as the constitution itself and the history of taxes in this land goes back to the days of British colonial rule. One thing, which must be remembered, is that tax law is directly connected with government revenues. Higher the taxes, greater the revenues. For this reason, taxes are used as a good source of government's income. Revenue collection is usually the most important purpose behind the imposition of a new tax or increase in the present ones. However revenue collection is not the sole objective even though it is certainly the most important one. There are other reasons for which taxes are either increased or decreased. Tax law is actually one of the very few fiscal measures that government has to control the financial markets. Apart from its main objective, which is revenue for the government, taxes also help in controlling economic activity in the country and are often used by the government to control the flow of money in the markets

DEFINITION:

Taxes are a defined as mandatory payments of the contributors to the budget and to the extra-budgetary funds in the amount determined by law and within the stipulated deadlines.

The functions of taxes are a manifestation of their essence; they are a means to represent the characteristics of taxes. The functions of taxation illustrate its social purpose of the value-based distribution and redistribution of income. Each of the functions fulfilled by the taxation instrument is a manifestation of an internal feature, an indicator or trait or this economic category.

There are five main functions of taxes: fiscal, redistributory, regulating, controlling, and promoting.

1. The main function of taxation is the fiscal one. It is through fiscality that taxes play their role in the formation of the state budget necessary for the realization of national and holistic state programmes. The fiscal function provides for the achievement of the main social goal of taxation—the formation of the state's financial resources necessary for executing the role of the latter (defence, social, environmental protection, etc.)

2. The allocation function of taxation expresses their essence as a special centralized instrument of allocation relations and consists of the social income redistribution among various groups of citizens: from wealthy to deprived ones, which ultimately provides for the assurance of the social stability of the population.

3. The regulatory function of taxation was initiated as soon as the state started to take active part in the economic set-up of the society. This function is aimed at achieving specific goals of the taxation policy through the taxation mechanism. Taxation regulation entails three sub-functions.
   - The stimulating sub-function is aimed at the development of special socio-economic processes, and is implemented through a system of allowances, exemptions and preference arrangements. The legislation in force stipulates the stimulation of a number of taxpayer categories such as the owners of small enterprises, the agricultural producers, capital investors, or charities.

   - The destimulating sub-function inhibits some socio-economic processes through the conscious exaggeration of the taxation burden. As a rule, the effect of this sub-function is related to the introduction of excessive tax rates.

   - These are, for example, the protectionist measures of the state, aimed at supporting local producers through prohibitive import custom duties. It is important to keep in mind, nevertheless, that taxation relations, as any other relations, must replicate continuously.

   - Taxes must be collected today, tomorrow and always. This is why the utilization of the destimulating sub-function should not lead to the weakening of the taxation basis, to suppression, or even to liquidation of the tax source. Such an exaggeration may result in a situation where there will be no income/processes to be taxed.

   - The replication (regeneration) function is explained as follows: by taxing the utilization of natural resources, roads, mineral and primary resources, the state uses these proceeds in order to regenerate the exploited resources.

4. The controlling function of taxation—through taxation, the state controls the financial-economic activity of juridical and natural persons. This also contributes to controlling the sources of income and the directions of spending.

5. The incentive function stipulates special taxation arrangements for a certain group of citizens, who are social achievers (participants in wars, etc.).

CHAPTER 03

Types of Taxes and Non-Tax Revenue

❖ **There are two types of taxes :**

1. **Direct taxes**
   - Income tax
   - Wealth tax
   - Corporate tax
   - Gift tax
   - Profession tax

2. **Indirect Taxes**
   - Sales tax
   - VAT (value added tax)
   - Central duty
   - Excise duty
   - STT (Security transaction tax)
   - Service Tax
   - Entertainment Tax

3. **Non-Taxes Revenue**
   - Fees
   - Fines
   - Penalties
   - Surplus from public enterprise
   - Special assessment of betterment
   - Grants and gifts
   - Deficit financing

Direct tax

Taxes in India are levied by the Central Government and the state governments. Some minor taxes are also levied by the local authorities such the Municipality or the Local Council. The authority to levy a tax is derived from the Constitution of India which allocates the power to levy various taxes between the Centre and the State. An important restriction on this power is Article 265 of the Constitution which states that "No tax shall be levied or collected except by the authority of law. Therefore each tax levied or collected has to be backed by an accompanying law, passed either by the Parliament or the State Legislature. In 2010-11, the gross tax collection amounted to 7.92 trillion, with direct tax and indirect tax contributing 56% and 44% respectively. Company's residents in India are taxed on their worldwide income arising from all sources in accordance with the provisions of the Income Tax Act. Non-resident corporations are essentially taxed on the income earned from a business connection in India or from other Indian sources. A corporation is deemed to be resident in India if it is incorporated in India or if it's control and management is situated entirely in India. Domestic corporations are subject to tax at a basic rate of 35% and a 2.5% surcharge. Foreign corporations have a basic tax rate of 40% and a 2.5% surcharge. In addition, an education cess at the rate of 2% on the tax payable is also charged. Corporate are subject to wealth tax at the rate of 1%, if the net wealth exceeds Rs.1.5 mn (apex. $ 33333). Domestic corporations have to pay dividend distribution tax at the rate of 12.5%; however, such dividends received are exempt in the hands of recipients. Corporations also have to pay for Minimum Alternative Tax at 7.5% (plus surcharge and education cess) of book profit as tax, if the tax payable as per regular tax provisions is less than 7.5% of its book profits.

Definition of income :

In order to tax the income of a person the term itself is designed under the Income Tax Act. As per the Act the term Income includes:

a. Profits and gains of Business or Profession: This includes income from carrying on a business or income earned by doing any profession.
b. Dividend:
c. Profit in lieu of Salary, perquisite: This includes any amount received by an employee from his employer other then the salary amount.
d. Allowances granted to the assesse to meet his expenses incurred for performance of his duties: This includes allowances such as HRA, Medical allowance, etc given by an employer to his employee.
e. Any capital gains: This means any profit derived on sale of any capital asset.
f. Winning from lotteries, crossword puzzles, races, card game, T.V. Show, etc
g. Any sum received for fund created for welfare of employees. One interesting thing in the definition of income is that it can be received in cash or in kind. More over the Income Tax Act does not make distinction between legal source of income or illegal source of income. This means that gambling, smuggling income is also chargeable to tax under the Income Tax act. More over gifts of personal nature for e.g. Birthday/ marriage gifts are not treated as income (but there are some exceptions in this. In all this one more thing is that the term income does not only means profits but there is a concept of negative income also.

Five heads of income.

1. Income under Head Salaries: This head taxes the income earned by an individual as salary from any firm or organisation Income under heads of salary is defined as remuneration received by an individual for services rendered by him to undertake a contract whether it is expressed or implied. According to Income Tax Act there are following

conditions where all such remuneration are chargeable to income tax:

- When due from the former employer or present employer in the previous year, whether paid or not.
- When paid or allowed in the previous year, by or on behalf of a former employer or present employer, though not due or before it becomes due.
- When arrears of salary is paid in the previous year by or on behalf of a former employer or present employer, if not charged to tax in he period to which it relates.

Income Comes Under Head of Salary

Under section 17 of the Income Tax Act, 1961 there are following incomes which comes under head of salary:

- Salary (including advance salary)
- Wages
- Fees
- Commissions
- Pensions
- Annuity
- Perquisite
- Gratuity
- Annual Bonus
- Income From Provident Fund
- Leave Encashment
- Allowance
- Awards

Leave Encashment:

Leave encashment is the salary received by an individual for leave period. It is a chargeable income whether he is a government employee or not. Under section 10(10AA) (i) there is also a provision of exemption in case of leave encashment depending upon whether he is a government employee or other employees.

Annuity:

It is an annual income received by the employee from his employer. It may be paid by the employer as voluntarily or on account of contractual agreement. It is not taxable until the right to receive the same arises. Under section 56, Income Tax Act, 1961 other annuities come under a will or granted by a life insurance company or accruing as a result of contract which comes as income under from other sources.

Gratuity:

It is salary received by an individual paid by the employee at the time of his retirement or by his legal heir in the case of death of the employee.

Allowance:

It is the amount received by an individual paid by his/her employer in addition to salary. Under section 15 of the Income Tax Act, 1961 these allowance are taxable excluding few conditions where they are entitled of deduction/ exemptions.

House Rent Allowance:

Under sections 10(13A) of Income Tax Act, 1961 allowance is defined as an amount received by an employee paid by his/ her employer as a rent of his/her house. It is a taxable income. There is no exemption in tax if he is living in his own house or house for which he is not paying rent. There are following amount which are exempt from tax:

- Actual house rent paid by that individual
- Rent paid for the accommodation over 10% of the salary
- 50% of the salary if house is placed at Delhi, Mumbai, Kolkata, Ↄ̇ Chennai 40% of the salary in it is placed in any other city

Entertainment Allowance:

It is the amount paid by employer for availing entertainment services.

Under section 16(ii) of Income Tax Act, 1961 it is entitled to deduction in tax from is salary. But in this case deduction is given to his gross salary which also includes entertainment allowance.

- Entertainment allowance received
- 20% of basic salary excluding any other allowance
- Rs. 5000 In case of other employee entitled to minimum deduction
- Entertainment allowance received
- 20% of basic salary excluding any other allowance Ↄ̇ Rs. 7500
- Entertainment allowance received during 1954-1955

Other Special Allowances

- Children Education Allowance
- Tribal Area Allowance
- Hostel Expenditure Allowance
- Remote Area Allowance

- Compensatory Field Area Allowance
- Counter Insurgency Allowance
- Border Area Allowance

Hilly Area Allowance Allowances for there is a provision of exempt in income tax are:

- Allowance given to a citizen of India, who is a government employee, for rendering services outside India
- Allowances given to Judges of High Courts
- Allowance given Judges of Supreme Court
- Allowances received by an employee of UNO

Perquisite :

Under section 17(2) of Income Tax Act, 1961 perquisite is defined as:

- Amount paid for the rent-free accommodation provided to the assessee by his employer
- Any concession in the matter of rent respecting any accommodation provided to the assessee by his employer
- Any benefit or amenity granted or provided free of cost or at concessional rate in any of the following cases:
  1. By a company to an employee, who is a director thereof
  2. By a company to an employee being a person who has a substantial interest in the company
  3. By any employer to an employee whose income under the head 'Salaries' exceeds Rs.24000 excluding the value of non monetary benefits or amenities
  4. Any sum paid by the employer in respect of any obligation which, but for such payment, would have been payable by the assessee
  5. Any sum payable by the employer whether directly or through a fund, other than a recognised provident fund or EPF, to effect an assurance on the life of the assessee or to effect a contract for an annuity.

There are following perquisites which are tax free:

- Medical facility.
- Medical reimbursement.
- Refreshments.
- Subsidised Lunch/ Dinner provided by employer • Facilities For Recreation
- Telephone Bills
- Products at concessional rate to employee sold by his/ her employer
- Insurance premium paid by employer
- Loans to employees by given by employer • Transportation

- Training
- House without rent
- Residence Facility to member of Parliament, judges of High Court/ Supreme Court
- Conveyance to member of Parliament, judges of High Court/ Supreme Court
- Contribution of employers to employee's pension, annuity schemes and group insurance

Income Deductions from Salary:

Certain deductions are available while determining the taxable salary income.

A) Standard Deduction

Income tax slabs (for Men) in India:

Income Tax Slab in (Rs)	Tax
0 To 2,00,000	NO TAX
2,00,001 To 5,00,000	10%
5,00,001 To 10,00,000	20%
Above 10,00,000	30%

Income tax slabs 2014-2015 (for Women) in India:

Income Tax Slab in (Rs)	Tax
0 To 2,00,000	NO TAX
2,00,001 To 5,00,000	10%
5,00,001 To 10,00,000	20%
Above 10,00,000	30%

Income tax slabs 2013-2015 (for Senior Citizens) in India:

Income Tax Slab in (Rs)	Tax
0 To 2,00,000	NO TAX
2,00,001 To 5,00,000	10%
5,00,001 To 10,00,000	20%
Above 10,00,000	30%

B) Professional Tax

Professional tax, which is paid, is allowed as deduction.

C) Arrears salary

If salary is received in arrears or in advance, it can be spread over the years to which it relates and be taxed accordingly as per section 89(1) of the Income tax Act.

2. Income from house property

What Is Heads of House Property?

According to Chapter 4, Section 22 - 27 of Income Tax Act, 1961 there is a provision of income under head of house property . In every section from 22-27 there are detail

specifications of house property income. It is defined as income earned by a person through his house or land.

What Income Comes Under Head of House Property:

Annual value of building or land owned by assessee. There is a charge on the potential of property to generate income not on the rent received. But if property is used for making profit in business then it will be taxable not under this head but will be taxable under head of profit in business.

How to calculate annual value of property:

According to annual value, house property is calculated as:

- Annual value of a house is zero if property is in the occupation of the owner for his residence for the whole year & if no other benefit is availed by owner from his property. There will be no deductions as given under section 24 except deduction interest on borrowed capital
- If the owner lets out the house or a part thereof for any period of time during the previous year the annual value of the property or part has to be calculated for the whole year and the proportionate annual value of the period for which the house or any part thereof was in the occupation of the owner for his own residence shall be deducted from the gross annual value. The assessee in such cases cannot claim deduction under section 24 in excess of the annual value so determined.
- The assesses occupies more than one house for his residence, the above exemption is applicable only to one such house at the option of the assessee. The annual value of the other house or houses shall be computed as if the house or houses are let.
- In case where the assessee has only one residential house but it cannot be occupied by the owner by reason of that owing to his employment, business or profession carried out on at any other place, he has to reside at that other place in a building not belonging to him, the annual value of such house shall be taken
- To be nil if the house is not actually let and no other benefit is derived by the owner from such house. The assessee cannot claim any deduction in such case as allowable under section 24 of the Act except for interest on borrowed capital subject to a maximum of Rs. 15,000/-

3. Income from Business/Profession:

- Profits and gains of assessee from any business or profession during assessment year.
- Any payment or compensation due or received by a person for his services to organization as a part of his business.
- Making profit in trade Income of professional or organization against services provided by that professional/ organization.
- Profits on sale of a license granted under the Imports (Control) Order, 1955, (EXIM control Act, 1947).
- Cash received or due by any person against exports under government schemes.
- Any benefit whether it is not in cash coming from business/ profession.
- Any profit, salary, bonus or commission received by company partners

4. Income from capital gain

Capital Gain:

According to Income Tax Act,1961 heads of capital gain is defined as gains derived on transfer of capital asset. Capital Gain is the profit or gain of an assessee coming from the transfer of a capital asset effected during the previous year or assessment year. "Capital Asset" and transfer are predefined in income tax act.

Capital Asset:

Under section 2(14) of the Income Tax Act,1961 Capital Asset is defined as property of any kind held by assesse including property held for his business or profession. It includes all type real property as well as all rights in property. It is also defined as gains on transfer of assets in which there in no cost of acquisition like:

- Goodwill of business generated by assessee
- Tenacy rights
- Stage carriage permits
- Loom hours
- Right to manufacture
- Processing & production of any article or things

Assets Which Don't Come Under Heads of Capital Assets

According to Income Tax Act, 1961 there are few assets which don't form a part of Capital Assets, which are as follows:

- Stock of goods and raw materials used by assessee for his business or profession

- Those property which are movable like wearing apparel, furniture, automobile, phone, household goods etc. Held by assessee. But Jewellery which is also an movable assets comes under heads of Capital Assets.

- Agricultural property in India. But agriculture land coming under municipal limits (in area having population ore than 10,000) comes under Capital Assets. Agriculture lands within 8 Km from municipal limit also comes under Capital Assets if it is notified by the central government of India

- Agricultural property in India. But agriculture land coming under municipal limits (in area having population ore than 10,000) comes under Capital Assets. Agriculture lands within 8 Km from municipal limit also comes under Capital Assets if it is notified by the central government of India

- Few Gold Bonds issued by government

- Few special bonds issued by central government like Special Bearer Bonds, 1991.

Transfer of Capital Assets:

Under Section 2(47) of The Income Tax Act, 1961 transfer of capital assets is defined as:

- Sale, exchange and relinquishment of assets
- Extinguishment of any rights in capital assets
- Acquisition of capital assets or rights
- Conversion of capital asset by its owner as stock in trade of his business, it may also be a term of transfer
- Transfer of immovable property under Section53A of Transfer ofProperty Act, 1882
- Any transaction by which an assessee become enable to act as a member of cooperative society
- Any transaction by which an assessee acquire shares in cooperative society.

5. Income from other sources : Every type of income comes under a specified heads. But there are few incomes, which don't come under any of following heads:

- Salary
- House Property
- Profit In Business/ Profession
- Capital Gains

  So under Section 56(2) of Income Tax Act, 1962 all such income comes in this heads of income. There are following incomes which are taxed under this heads.
- Income coming as a dividend paid by a company to an assese.

- Income coming from winning in lottery, crossword puzzles, races, card games, gambling or other such sports.
- Income coming as an amount received by assessee from his employer as a fund for welfare of employee.
- Income as an interest on securities.
- Income coming by letting on hire machinery, plant, furniture, building or other goods Income coming from insurance policy

Wealth Tax

Wealth tax is charged for every assessment year in respect of net wealth. Wealth tax is also a direct tax just like income tax computed on net wealth of an assessee. But it is charged on the amount of net wealth exceeding Rs. 15 Lacs. Rate of wealth tax is 1%. Wealth tax is charged on the net wealth of an assessee valued as on valuation date. The valuation date for chargeability of wealth tax is 31st March of the financial year.

1) Building:

Any building or land appurtenant thereto u/s2 (ea) (i) is treated as an asset and it includes:

a) Commercial building

b) Residential building

c) Any guest house

d) A farmhouse situated within 25 kilometres from the local limits of a local authority

However following buildings are not treated as assets:

a. A house meant for residential purposes is allotted by a company to an employee or an officer or a whole time director, having a gross annual salary of less than Rs.5lakhs
b. Any house for residential or commercial purposes, which forms part of stock in-trade
c. Any house occupied by assessee for the purposes of his own business or profession
d. Any residential property that has been let out for a minimum period of 300days in the previous year2008

e. Any property in the nature of commercial establishments or complexes

2) Motor Cars Sec:

Any motorcar is an asset except the following :

a) Motor cars used by the assessee in the business of running them on hire

b) Motor cars held as stock- in- trade

3) Jewellery,

Bullion, Utensils Of Gold, Silver etc. Jewellery, bullion furniture, utensils or any other article made wholly or partly of gold, silver, platinum, or any other precious metal of any alloy containing one or more of such precious metals are treated as an asset

For this purpose, the term jewellery includes

a) Ornaments made of gold, silver, platinum or any other precious metal of any alloy containing one or more of such precious metals, whether or not containing any precious or semi precious stone, whether or not set in any furniture, utensils, or other articles or worked or sewn into any wearing apparel.

b) Precious or semi precious stones, whether or not set in any furniture, utensils or other articles or worked or sewn into any wearing apparel However, the term jewellery shall not include the Gold Deposit Bonds issued under Gold Deposit Scheme, 1999 notified by the Central Government However, if any of the above stated assets are held by the assesses as stock-in trade, then it is not treated as an asset

4) Yachts, Boats and Aircrafts SeaYachts, boats and aircrafts are treated as "assets" excluding yachts boats and aircrafts used by assessee for commercial purposes.

5) Urban Land : Urban land is treated as an "asset" and urban land means land situated.

a) in any area which is comprised within the jurisdiction of local authority and which has a population of not less than ten thousand according to the last preceding figures of census of which the relevant figures have been published before the valuation date;

b) any area within such distance, not being more than 8 kilometer from the local limits of the local authority as the central government may, having regard to the extent, and scope for

urbanization of that area and other relevant considerations, specified in this behalf by notification in the official gazette. However land is not treated as "asset" in the following cases:

a) Land on which construction of a building is not permissible under any

law for the time being in force in the area in which such land is situated;

b) Land occupied by any building which has been constructed with approval of the appropriate authority;

c) Any unused land held by the assessee for industrial purposes for a period of two years from the date of acquisition by him

d) Land held by an assessee as stock-in-trade for a period of 10 years from the date of its acquisition by him.

6) Cash-in-hand

Following is treated as an "assets":

a. In case of any individual and HUF, cash in hand on the last moment of the valuation date in excess of 50,000 shall be treated as "asset"
b. In case of any other person any amount not recorded in the books of accounts shall be treated as "asset".

CHAPTER-4

PROFESSIONAL TAX

In India, this tax is imposed by various states. It is imposed on business owners, working individuals, merchants and people carrying out various occupations. The following states impose this levy in India -Karnataka, West Bengal, Andhra Pradesh, Maharashtra, Tamilnadu, Gujarat, and Madhya Pradesh. Professional tax is levied by particular Municipal Corporations and majority of the Indian states impose this duty. It is a source of revenue for the government. The maximum amount payable per year is ` 2,400/- and in line with your salary, there are predetermined slabs. It is paid by every member of staff employed in private companies. It is subtracted by the employer each month and sent to the Municipal Corporation. It is compulsory as income tax. You will be eligible for income tax deduction for this payment.

Criteria in various states of India

In Maharashtra, this duty is applicable both on individuals and companies as laid down by the guidelines of the Maharashtra Professional Tax Act of 1975.

Every individual living in Maharashtra, involved in any business,

profession, occupation or employment is legally responsible to pay it and has to get a Certificate of Enrolment from the Professional Authority. As soon as you receive this certificate, you can fulfill your personal tax liability for 5 years by making a one-time payment, which is equivalent to the sum of Professional Tax for 4 years beforehand, getting relief for payment of one year. In Tamil Nadu, it is imposed by the Municipal Council on businessmen, professionals, and employed individuals.

Every company which conducts business and every individual, who is involved directly in any business, occupation, or employment in the town panchayat on the first day of the half-year for which return has been submitted, needs to pay biannual tax at the rates stipulated.

Professional Tax Slabs in Various States in West Bengal

Income	**Tax To be Imposed**
Up to 1,500	Nil
From 1501 to 2001	18
From 2001 to 3001	25
From 3001 to 5001	30
From 5001 to 6001	40
From 6001 to 7001	45
From 7001 to 8000	50
From 8001 to 9000	90
From 9001 to 15,000	110
From 15,001 to 25,000	130
From 25,001 to 40,000	50
Beyond 40,001	200

In Maharashtra

Income	Tax To be Imposed
Up to 21000	Nil
From 21001 to 30000	75%
From 30001 to 45000	188%
From 45000 to 60,000	390%
From 60,001 to 75,000	585%
More than 75,001	810%

In Tamil Nadu

Income	Tax To be Imposed
Up to 2000	Nil
From 2500 to 3500	60%
From 3500 to 5000	120%
From 5000 to 10,000	175%
More than 10,000	200%

In New Delhi

Income	Tax To be Imposed
Up to 1,10,000	Nil
From 1,10,00 to 1,45,000	Nil
From 1,45,000 to 1,50000	10%
From 1,50,000 to 1,950,000	20%
From 1,95,000,to 2,50,000	20%
More than 2,50,000	30%

Corporation Tax:

Corporation Tax is charged on all profits (income and gains), wherever arising, of companies resident in the State, with some exceptions, and non-resident companies who trade in the State through a branch or agency.

Company Taxed :

Companies pay Corporation Tax. This tax is charged on the company's profits which include both income and chargeable gains. A company's income for tax purposes is calculated in accordance with Income Tax rules. Chargeable gains are calculated in accordance with Capital Gains Tax rules.

Rate of Corporation Tax:

There are two rates of Corporation Tax: Excepted trades include certain land dealing activities, income from working minerals and petroleum activities

How do I decide whether to trade as a Sole Trader or as a Company

Your own individual circumstances will dictate whether you should operate as a limited company or as a sole trader. In addition to the taxation issues you need to consider there are various other practical and legal matters which should be taken into account when setting up a company and on which you should seek professional advice.

Many countries impose corporation tax or company tax on the income or capital of some types of legal entities. A similar tax may be imposed at state or lower levels. The taxes may also be referred to as income tax or capital tax. Entities treated as partnerships are generally not taxed at the entity level. Most countries tax all corporations doing business in the country on income from that country. Many countries tax all income of corporations organized in the country. Company income subject to tax is often determined much like taxable income for individuals. Generally, the tax is imposed on net profits. In some jurisdictions, rules for taxing companies may differ significantly from rules for taxing individuals. Certain corporate acts, like reorganizations, may not be taxed. Some types of entities may be exempt from tax.

Many countries tax corporate entities on income and also tax the owners when the corporation pays a dividend. Where the owners are taxed, a withholding tax may be imposed. Generally, these taxes on owners are not referred to as corporate tax.

Gift Taxes:

Estate planning is the process of transferring wealth wealth to subsequent generation Techniques involve planning for transfers at death and during life. One such mechanism is the gift, or right to transfer assets to another person while the donor is still alive, with the goal of reducing one's taxable estate. In certain instances when all available exemptions, exclusions and thresholds have been met, these transfers are subject to a gift tax.

Types of gifts include :

- **Direct:** the donor transfers cash or property directly to the done.
- **Indirect:** the donor makes a transfer for the donee's benefit. Troypays his girlfriend's credit card balance, as an example.
- **Complete:** in making a transfer to the donee, the donor gives up allright and dominion over the property.
- **Incomplete:**
  in making a transfer to the donee, the donor fails to give up all control over the property. If Helmut places money into a revocable trust, then he has made an incomplete gift as he retains the right to control the ultimate disposition of what is in the trust. By contrast, should the trust become irrevocable, then its contents constitute a completed gift.

- **Reversionary Interest:**
  gifts that the donor transfers to the done which revert back to the donor. Their worth to the donee is their present value rather than fair market value. An example would be when a donor places money in a trust for a specific time period for the donee's benefit. At the end of the term, the money or property reverts back to the donor. The value of the gift is less than the value of the property in this instance.

- **Net Gift:** whereas in most instances the donor is responsible for any gift tax, in the case of a net gift, the donee would be.

Gift Valuation

For gift tax purposes, the value of the gift is its fair market value on the date of its transfer to the donee. Real estate and collectibles would require an appraisal. A bond would be valued as

the present value of its future payments. The value of publicly traded shares would be the average of the high and low share price for the day on which they are gifted.

Indirect tax :

In the colloquial sense, an indirect tax (such as sales tax, a specific tax [a tax per unit], value added tax (VAT), or goods and services tax (GST)) is a tax collected by an intermediary (such as a retail store) from the person who bears the ultimate economic burden of the tax (such as the consumer). The intermediary later files a tax return and forwards the tax proceeds to government with the return. In this sense, the term indirect tax is contrasted with a direct tax which is collected directly by government from the persons (legal or natural) on which it is imposed. Some commentators have argued that "a direct tax is one that cannot be shifted by the taxpayer to someone else, whereas an indirect tax can be." An indirect tax may increase the price of a good so that consumers are actually paying the tax by paying more for the products. Examples would be fuel, liquor, and cigarette taxes. An excise duty on motor cars is paid in the first instance by the manufacturer of the cars; ultimately the manufacturer transfers the burden of this duty to the buyer of the car in form of a higher price. Thus, an indirect tax is such which can be shifted or passed on. The degree to which the burden of a tax is shifted determines whether a tax is primarily direct or primarily indirect.

CHAPTER 05

VALUE ADDED TAX

VALUE ADDED TAX

Value Added Tax is a broad-based commodity tax that is levied at multiple stages of production. The concept is akin to excise duty paid by he manufacturer who, in turn, claims a credit on input taxes paid. Excise duty is on manufacture, while VAT is on sale and both work in the same manner, according to the white paper on VAT released by finance minister Chidambaram. The document was drawn up after all states, barring UP, were prepared to implement VAT from April. It is usually intended to be a tax on consumption, hence the provision of a mechanism enabling producers to offset the tax they have paid on their inputs against that charged on their sales of goods and services. Under VAT revenue is collected throughout the production process without distorting any production decisions.

WHY VAT IS PREFERRED OVER SALES TAX

While theoretically the amount of revenue collected through VAT is equivalent to sales tax collections at a similar rate, in practice VAT is likely to generate more revenue for government than sales tax since it is administered on various stages on the production - distribution chain. With sales tax, if final sales are not covered by the tax system e.g. due to difficulty of covering all the retailers, particular commodities may not yield any tax. However, with VAT some revenue would have been collected through taxation of earlier transactions, even if final retailers evade the tax net. There is also in-built pressure for compliance and auditing under VAT since it will be in the interest of all who pay taxes to ensure that their eligibility for tax credits can be demonstrated. VAT is also a fairer tax than sales tax as it minimizes or eliminates the problem of tax cascading, which often occurs with sales tax. These are facilitated by the fact that VAT operates through a credit system so that tax is only applied on value added at each stage in the production - distribution chain. At each intermediate stage credit will be given for taxes paid on purchases to set against taxes due on sales. Only at consumption stage where there are no further transactions will there be no tax credits. Lack of input credit facility in sales tax often results in tax on inputs becoming a cost to businesses which are often passed on to consumers. Sales tax is often applied again to the sales tax element of the cost, thus there is a problem of tax on tax. This is not the case with VAT, which makes it a neutral tax as it provides the least disturbance to patterns of production and the generation and use of income

In addition, the audit trail that exists under the VAT system makes it a more effective tax in administration terms than sales tax as it helps with the verification of VAT amounts declared as due. This is made possible by the fact that one person’s output is another’s input. As with

sales tax imports are treated the same way as local goods while exports are zero- rated to avoid anti-export bias.

Notwithstanding the advantages mentioned above, it is worth noting that VAT is a considerably complex tax to administer compared with sales tax. It may be difficult to apply to small companies due to difficulties of record keeping and its coverage in agriculture and the services sector may be limited. To cover the high administration costs, VAT rates of 10-20 per cent are generally recommended. The equity impact of the relatively high rates have been a cause for concern as it is possible that the poor spend relatively high proportions of their incomes on goods subject to VAT. Thus the concept of zero VAT rate on some items has been introduced.

DIFFERENCE BETWEEN VAT AND CST

Under the CST Act, the tax is collected at one stage of purchase or sale of goods. Therefore, the burden of the full tax bond is borne by only one dealer, either the first or the last dealer. However, under the VAT system, the tax burden would be shared by all the dealers from first to last. Then, such tax would be passed upon the final consumers. Under the CST Act, the tax is levied at a single point. Under the VAT system, the retailers are not subject to tax except for the retail tax. Under the CST Act, general and specific exemptions are granted on certain goods while VAT does not permit such exemptions. Under the CST law, concessional rates are provided on certain taxes. The VAT regime will do away with such concessions as it would provide the full credit on the tax that has been paid earlier. Under VAT law, first, the dealer pays tax on the sale or purchase of goods. The subsequent dealer pays tax on the portion of the value added upon such goods. Thus, the tax burden is shared equally by the last dealer. To illustrate the whole procedure of VAT, an example is as follows At the first point of sale, the value of goods is Rs.100. The tax on this is 12.5%. Therefore, the net VAT would be 12.5%. At the second change of sale, the sale value is Rs.120 and the tax thereon is 15%. The tax that is to be paid at every point is 15%. The input tax is 15%. The dealer will get a credit for first change in sale of 2.5%-- i.e. 15% -12.5%. Therefore, 2.5% will be the net rate. At the third change of sale, the sale value is Rs.150 and the tax on this is 18.75%. At the last stage, the tax paid is 18.75%. The Input Tax is 18.75%. Dealer’s get a credit for second change in sale? I.e. 18.75% -15% = 3.75%. Therefore, 3.75% would be the net VAT. This means that VAT is paid in the last point tax under the sale tax regime.

WHO GAINS:

State and Central governments gain in terms of revenue. VAT has in-built incentives for tax compliance — only by collecting taxes and remitting them to the government can a seller claim the offset that is due to him on his purchases. Everyone has an incentive to buy only from registered dealers — purchases from others will not provide the benefit of credit for the taxes paid at the time of purchase. This transparency and in-built incentive for compliance would increase revenues. Industry and trade gain from transparency and reduced need to interact with the tax personnel. For those who have been complying with taxes, VAT would be a boon that reduces the cost of the product to the consumer and boosts competitiveness. VAT would be major blow for tax evaders, both manufacturers who evade excise duty payments and traders who evade sales-tax.

WHO PAYS:

All dealers registered under VAT and all dealers with an annual turnover of more than Rs 5 lakh will have to register. Dealers with turnovers less than Rs 5 lakh may register voluntarily.

HOW TO PAY:

VAT will be paid along with monthly returns. Credit will be given within the same month for entire VAT paid within the state on purchase of inputs and goods. Credit thus accumulated over any month will be utilized to deduct from the tax collected by the dealer during that month. If the tax credit exceeds the tax collected during a month on sale within the state, the excess credit will be carried forward to the next month.

WHICH GOODS WILL BE TAXABLE UNDER VAT

All goods except those specifically exempt. In fact, over 550 items will be covered under the new tax regime, of which 46 natural and unprocessed local products would be exempt from VAT. About 270 items, including drugs and medicines, all agricultural and industrial inputs, capital goods and declared goods would attract 4% VAT. But,following opposition from some states, it was decided that states would have option to either levy 4% or totally exempt food grains from VAT but it would be reviewed after one year. Three items — sugar, textile, tobacco — under additional excise duties will not be under VAT regime for one year but existing arrangement would continue.

VAT EFFECT ON ECONOMIC GROWTH

Economic growth can be facilitated through investment by both government and the private sector. Savings by both parties are required in order to finance investment in a non-inflationary manner. Compared to other broadly based taxes such as income tax VAT is neutral with respect to choices on whether to consume now or save for future consumption. Although VAT reduces the absolute return on saving it does not reduce the net rate of return on saving. Income tax reduces the net rate of return as both the amount saved as well as the return on that saving are subject to tax. In this regard VAT may be said to be a superior tax in promoting economic growth than income tax. Since VAT does not influence investment decisions on firms, by increasing their costs, its effects on investment can be said to be neutral.

FEATURES OF VAT

1. Rate of Tax VAT proposes to impose two types of rate of tax mainly:

- 4% on declared goods or the goods commonly used.
- 10-12% on goods called Revenue Neutral Rates (RNR). There would be no fall in such remaining goods.
- Two special rates will be imposed-- 1% on silver or gold and 20% on liquor. Tax on petrol, diesel or aviation turbine fuel are proposed to be kept out from the VAT system as they would be continued to be taxed, as presently applicable by the CST Act.

2. Uniform Rates in the VAT system, certain commodities are exempted from tax. The taxable commodities are listed in the respective schedule with the rates. VAT proposes to keep these rates uniform in all the states so the goods sold or purchased across the country would suffer the same tax rate. Discretion has been given to the states when it comes to finalizing the RNR along with the restrictions. This rate must not be less than 10%. This will ensure by doing this that there will be level playing fields to avoid the trade diversion in connection with the different states, particularly in neighbouring states.

3. No concession to new industries Tax Concessions to new industries is done away with in the new VAT system. This was done as it creates discrepancy in investment decision. Under the new VAT system, the tax would be fair and equitable to all.

4. Adjustment of the tax paid on the goods purchased from the tax payable on the goods of sale All the tax, paid on the goods purchased within the state, would be adjusted against the tax, payable on the sale, whether within the state or in the course of interstate. In case of export, the tax, paid on purchase outside India, would be refunded. In

case of the branch transfer or consignment of sale outside the state, no refund would be provided.

5. Collection of tax by seller/dealer at each stage. The seller/dealer would collect the tax on the full price of the goods sold and shows separately in the sell invoice issued by him.

6. VAT is not cascading or additive though the tax on the goods sold is collected at each stage, it is not cascading or additive because the net effect would be as follows: - the tax, previously paid on the sale of goods, would be fully adjusted. It will be like levying tax on goods, sold in the last state or at retail stage.

BIGGEST ADVANTAGE?

The biggest benefit of VAT is that it could unite India into a large common market. This will translate to better business policy. Companies can start optimizing purely on logistics of their operations, and not on based on tax-minimization. Lorries need not wait at check-points for days; they can zoom down the highways to their destinations. Reduced transit times and lower inventory levels will boost corporate earnings. Following are the some more advantage of VAT: -

Simplification Under the CST Act, there are 8 types of tax rates-1%, 2%, 4%, 8%, 10%, 12%, 20% and 25%. However, under the present VAT system, there would only be 2 types of taxes 4% on declared goods and 10-12% on RNR. It also helps to determine the relevant stage of the tax. This is necessary as the CST Act stipulates that the tax levies at the first stage or the last stage differ. Consequently, the question of which stage of tax it falls under becomes another reason for litigation. Under the VAT system, tax would be levied at each stage of the goods of sale or purchase.

2. Adjustment of tax paid on purchased goods Under the present system, the tax paid on the manufactured goods would be adjusted against the tax payable on the manufactured goods. Such adjustment is conditional as such goods must either be manufactured or sold. VAT is free from such conditions.

3. Further such adjustment of the purchased goods would depend on the amount of tax that is payable. VAT would not have such restrictions. CST would not have the provisions on refund or carry over upon such goods except in case of export goods or goods, manufactured out of the country or sale to registered dealer.Similarly, on interstate sale on tax-paid goods, no refund would be admissible. This is because the amount of tax, which the goods have

suffered, is not known at the subsequent stage. In the VAT system, the amount of tax would be known at each and every stage of goods of sale or purchase.

4. **Fair and Equitable** VAT introduces the uniform tax rates across the state so that unfair advantages cannot be taken while levying the tax.

5. **Procedure** of simplification Procedures, relating to filing of returns, payment of tax, furnishing declaration and assessment are simplified under the VAT system so as to minimize any interface between the tax payer and the tax collector.

6. **Minimize the Discretion** the VAT system proposes to minimize the discretion with the assessing officer so that every person is treated alike. For example, there would be no discretion involved in the imposition of penalty, late filing of returns, and non-filing of returns, late payment of tax or non payment of tax or in case of tax evasion.

7. **Computerization** the VAT proposes computerization which would focus on the tax evaders by generating Exception Report. In a large number of cases, no processing or scrutiny of returns would be required as it would free the tax compliant dealers from all the harassment which is so much a part of assessment. The management information system, which would form a part of integral computerization, would make the tax department more efficient and responsive.

VALUE ADDED TAX IN MAHARASHTRA:

Quick Flash Back

Sales tax was first introduced in India in the then Bombay Province as early as March 1938 where a tax was imposed on sale of tobacco within certain urban and suburban areas. In the year 1946, a general sales tax was introduced levying sales tax at the last stage of sale of goods.

The Bombay Sales Tax Act, 1959 introduced in 1959 underwent many changes thereafter and in July 1981, first point tax was introduced

wherein goods were classified into three main schedules, broadly covering tax free goods, intermediate products and finished goods. The BST Act was repealed and Maharashtra Value Added Tax Act, 2002 came into force we.f. 1st April, 2005 to usher in the progressive value added tax system in place of the old sales tax system.

VAT is a progressive and transparent system of taxation which eliminates the cascading impact of multiple taxation through a multipoint taxation and set-off principle. It promotes

transparency, compliance and equity and therefore, is both dealer friendly and consumer friendly.

VAT being a multi point tax, envisages an increase in the number of dealers and is based on the concept of self-assessment and selfcompliance. It is therefore, inevitable that the Sales Tax Department transforms itself into a dealer friendly, focused and dynamic department to cater to the ever increasing expectations of both the Government and the Trade & Industry.

Sales Tax Department has taken up the challenge to transform their selves and be available for assisting the dealers in complying with the provisions of the law. They are in the process of installing a state-wide networked IT system to computerise entire tax administration and hope to provide online service to the dealers in due course. They are also realigning their organisational structure to meet the challenges of the new system and stakeholders' expectations.

Sales Tax in India

Sales tax is levied on the sale of a commodity which is produced or imported and sold for the first time. If the product is sold subsequently without being processed further, it is exempt from sales tax.

Sales tax can be levied either by the Central or State Government, Central Sales tax department. Also, 4 per cent tax is generally levied on all inter-State sales. State sales taxes, that apply on sales made within a State, have rates that range from 4 to 15 per cent. Sales tax is also charged on works contracts in most States and the value of contracts subject to tax and the tax rate vary from State to State. However, exports and services are exempt from sales tax. Sales tax is levied on the seller who recovers it from the customer at the time of sale.

Sales Tax in India is that form of tax which is imposed by the government on sale/purchase of a particular commodity within the country. It is imposed under Central Government (Central Sales Tax) and the State Government (Sales Tax) Legislation. Normally, each state has its own sales tax act and levies the tax at various rates. Apart from sales tax, certain states also impose extra charges such as works contracts tax, turnover tax & purchaser tax. Thus, sales tax plays a major role in acting as a major generator of revenue for the various State Governments. Under the sales tax which is an indirect form of tax, it is the responsibility of seller of the commodity to collect or recover the tax from the purchaser. Generally, the sale of imported items as well as sale by way of export is not included in the range of commodities that require payment of sales tax. Moreover, luxury items (such as cosmetics) are levied higher sales tax rates. The Central Sales Tax (CST) Act that comes

under the direction of Central Government takes into consideration all the interstate sales of commodities.

Hence, we see that sales tax is to be paid by every dealer when he sells any commodity, during inter-state trade or commerce, irrespective of the fact that there may be no liability to pay tax on such a sale of goods under the tax laws of the appropriate state. Sales tax is to be paid to the sales tax authority of the state from which the movement of the commodities starts or commences.

Central excise duty

In India, excise duty is being imposed in accordance with Central Excise Act 1944 which happens to be the basic act to regulate laws related to Central Excise Duty. This act has given the central government, a power to make rules and laws for pursuing this act. Thus, central government has made a following set of rules under this act.

- The Central Excise (Advance Rulings) rules, 2002
- The Central Excise (Removal of Goods at Concessional Rate of Duty for
- Manufacture of Excisable Goods) Rules, 2001
- The Central Excise Rules, 2002 (Section 143 of the Finance Act, 2002)
- The Central Excise (Settlement of Cases) Rules, 2001
- The Central Excise (Settlement of Cases) Rules, 2001
- Central Excise Valuation (Determination of Price of Excisable Goods)
- Rules, 2000
- Consumer Welfare Fund Rules, 1992
- The Central Excise (Settlement of Cases) Rules, 2001
- Central Board of Excise and Customs (CBEC) is the whole sole in-charge of taking care of everything related to Central Excise Law and this department works under the Ministry Of Finance of Government of India.

This department regulates all the tasks of formulizing the policies related to following actions.

- Levy and collection of customs and central excise duties
- Prevention of smuggling
- Administering matters related to customs

Account Head	Duty Type	Basic Head Description
0038003	CENVAT	BASIC EXCISE DUTIES(CENVAT)
00380013	SED	SPECIAL EXCISE DUTIES (SCHEDULE – 2 OF CETA)
00380018	AED(GSI)	ADDITIONAL EXCISE DUTIES IN LIEU OF SALES TAX
00380027	AED(TTA)	ADDITIONAL EXCISE DUTIES ON TEXTILE & TEXTILE ARTICLES
00380037	CESS	CESS ON JUTE
00380039	CESS	CESS ON TEA
00380056	CESS	CESS ON BIRI
00380059	CESS	CESS ON TOBACCO
00380062	CESS	CESS ON CRUDE OIL
00380065	CESS	CESS ON SUGAR
00380072	CESS	CESS ON PAPER
00380078	CESS	CESS ON AUTOMOBILE
00380084	CESS	CESS ON OTHER COMMODITIES
00380087	DIFF - TOTAL	OTHER RECEIPTS
00380101	ADE	ADDITIONAL EXCISE DUTIES ON INDIGENOUS MOTOR SPIRIT
00380102	ADE	ADDITIONAL EXCISE DUTIES ON HIGH SPEED DIESEL OIL
00380106	NCCD	NATINAL CALAMITY CONTINGENCY DUTY

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inistering central excise and narcotics to the extent which has beengiven to this department

This department also acts as chief administrative authority for many subordinate departments like Custom Houses, Central Excise offices and Central Revenues Control Laboratory.

In actual terms, Central Excise Duty is an indirect form of tax which is levied on goods and services which are manufactured inside India and are to be used in India only. The central excise department's responsibility arises as soon as the goods or the services are manufactured. The department has to levy manufacturing tax from the manufacturer which is passed on to the consumers by the manufacturers.

The goods that are being taxed under excise duty are actually those goods that have been mentioned in the first and the second schedule of the Central Excise Tariff Act 1985. In the recent announcement in Central Budget 2012, the general excise duty rate has been increased to 12% which was 10% earlier. Also the merit rate which was 5% has been raised to 6%. The excise duty which was applicable on around 130 commodities has been increased to 2% from previous rate of 1%. The tariff rate of central excise has been reduced for non-petroleum products to 12%. It has been decided that until the recommendation of finance bill 2012 are brought into act, the general excise rate of 12% and 6% will be maintained.

Excise

In the Indian tax structure, there are a lot of taxes that people pay for different reasons. Income tax, sales tax, entertainment tax, value added tax etc. All these taxes are existent because in some way or the other it impacts and helps the economy. One such tax that is prevalent in any manufacturing sector is the excise duty.

Excise duty

An excise or excise tax (sometimes called an excise duty) is a type of tax charged on goods produced within the country (as opposed to customs duties, charged on goods from outside the country). It is a tax on the production or sale of a good. This tax is now known as the Central Value Added Tax (CENVAT).

Though the collection of tax is to augment as much revenue as possible to the government to provide public services, over the years it has been used as an instrument of fiscal policy to stimulate economic growth. Thus it is one of the socio-economic objectives.

Types of excise duty

There are three different types of central excise duties which exist in India which are as follows:

Basic - Excise Duty, imposed under section 3 of the 'Central Excises and Salt Act' of 1944 on all excisable goods other than salt produced or manufactured in India, at the rates set forth in the schedule to the Central Excise tariff Act, 1985, falls under the category of basic excise duty in India.

Additional - Section 3 of the 'Additional Duties of Excise Act' of 1957 permits the charge and collection of excise duty in respect of the goods as listed in the schedule of this act. This tax is shared between the central and state governments and charged instead of sales tax.

Special - According to Section 37 of the Finance Act, 1978, Special Excise Duty is levied on all excisable goods that come under taxation, in line with the Basic Excise Duty under the Central Excises and Salt Act of 1944. Therefore, each year the Finance Act spells out that whether the Special Excise Duty shall or shall not be charged, and eventually collected during the relevant financial year.

Excisable goods

The term 'excisable goods' means the goods which are specified in the first schedule and the second schedule to the Central Excise Tariff Act, 1985, as being subject to a duty of excise and includes salt.

Who is liable to pay excise duty?

The liability to pay tax excise duty is always on the manufacturer or producer of goods. There are three types of parties who can be considered as manufacturers:

- Those who personally manufacture the goods in question
- Those who get the goods manufactured by employing hired labour
- Those who get the goods manufactured by other parties

Is it mandatory to pay duty on all goods manufactured?

Yes, it is mandatory to pay duty on all goods manufactured, unless exempted. For example, duty is not payable on the goods exported out of India. Similarly exemption from payment of duty is available, based on conditions such as kind of raw materials used, value of turnover (clearances) in a financial year, type of process employed etc.

What is the consequence of evading payment of excise duty

Under the different sections of the central excise act, the fines for evading tax can range from twenty-five to fifty per cent of the amount of duty evaded. When you look at the amount of excise you may have to pay, this is a rather large amount and along with the financial repercussions, you also have to encounter a tarnished image.

SECURITIES TRANSACTION TAX (STT) is applicable to the purchase or sale of equity shares, derivatives, units of equity-oriented funds through a recognised stock exchange in India or the sale of a unit of an equity-oriented fund to a mutual fund. With effect from 1 June 2006, the STT is payable equally by the

purchaser and seller at 0.125% of the transaction value on delivery based transactions. On non-delivery based transactions in equities or units of an equity oriented fund it is payable by the seller at 0.025%. In case of sale of options in securities, STT is levied at the rate of 0.017% of the option premium to be paid by the seller. In case of sale of options in securities where the option is exercised, STT is levied at 0.125% of the settlement price and is paid by the purchaser. In case of sale of futures in securities, STT at 0.017% is to be paid by the seller. In the case of sale of units of an equity oriented fund to the mutual fund, it is payable by the seller at 0.25%.However, with effect from Oct 1,2009 STT will not be applicable in respect of transactions entered into by any person for or on behalf of New Pension System Trust. The transaction value is determined as follows:

1. Options - Aggregate of strike price and premium of the option
2. Futures - the traded price
3. Other Securities - Sale/ Purchase Price

Service Tax

Service Tax is a form of indirect tax imposed on specified services called "taxable services". Service tax cannot be levied on any service which is not included in the list of taxable services. Over the past few years, service tax been expanded to cover new services. The objective behind levying service tax is to reduce the degree of intensity of taxation on manufacturing and trade without forcing the government to compromise on the revenue needs. The intention of the government is to gradually increase the list of taxable services until most services fall within the scope of service tax. For the purpose of levying service tax, the value of any taxable service should be the gross amount charged by the serviceprovider

for the service renderedby him.Service Tax was first brought into force with effect from 1 July 1994. All service providers in India, except those in the state of Jammu and Kashmir, are required to pay a Service Tax in India. Initially only three services were brought under the net of service tax and the tax rate was 5%. Gradually more services came under the ambit of Service Tax. The rate of tax was increased from 5% to 8% w.e.f 14 May 2003. From 10 September 2004 the rate of Service Tax was enhanced to 10% from 8%. Besides this 2% education cess on the amount of Service Tax was also introduced. In the Union Budget of India for the year 2006-2007, service tax was increased from 10% to 12%. On February 24, 2009 in order to give relief to the industry reeling under the impact of economic recession, The rate of Service Tax was reduced from 12 per cent to 10 per cent.

Some of the major services that come under the ambit of Service Tax are:

- Telephone
- Stockbroker
- General Insurance
- Advertising agencies
- Courier agencies
- Consulting engineers
- Custom house agents
- Steamer agents
- Clearing & forwarding agents
- Air travel agents
- Tour operators
- Rent-a-Cab Operators
- Manpower recruitment Agency
- Mandap Keepers
- Architects
- Interior Decorators
- Management Consultants
- Practicing Chartered Accountants
- Practicing Company Secretaries
- Practicing Cost Accountants
- Real Estates Agents/Consultants
- Credit Rating Agencies
- Private Security Agencies
- Market Research Agencies
- Underwriters Agencies
- Scientific and technical consultancy service
- Photography
- Convention
- Telegraph
- Telex

- Facsimile
- Online information and database access or retrieval Video-tape production
- Sound recording
- Broadcasting
- Insurance auxiliary activity
- Banking and other financial services
- Port
- Authorised Service Stations
- Leased circuits Services
- Auxiliary services to life insurance
- Cargo handling
- Storage and warehousing services
- Event Management
- Cable operators
- Beauty parlours
- Health and fitness centres
- Fashion designer
- Rail travel agents
- Dry cleaning services
- Commercial vocational institute, coaching centres and private tutorialsTechnical testing and analysis (excluding health & diagnostictesting) technical inspection and certification service
- Maintenance & repair services
- Commission and Installation Services
- Business auxiliary services, namely business promotion and Support services (excluding on information technology services) Internet café
- Franchise Services
- Out door Caterer’s service
- Airport Services
- Transport of Goods by Air Services
- Business Exhibition Services
- Intellectual Property Services
- Opinion Poll Services
- TV or Radio Programme Services
- Survey and Exploration of Minerals Services
- Travel Agent's Services other than Rail and Air travel agents Forward Contract Services
- Transport of goods through pipe line or other conduit Service Site preparation & clearance Services
- Dredging Services
- Survey & Mapmaking Services
- Cleaning Services
- Membership of Clubs & Associations
- Packaging Services
- Mailing list compilation & Mailing Services

CHAPTER-6

ENTERTAINMENT TAX IN INDIA

In India, entertainment tax is levied on every financial transaction that is related to entertainment such as movie tickets, major commercial shows and big private festivals. As per the Indian Constitution, entertainment is included in List 2. This revenue is reserved primarily for the state governments.

Following are some other forms of entertainment that are included in the purview of entertainment taxes:

Entertainment tax in India (overview)

In the pre-independence era, the British government levied huge taxes on events centered on entertainment or amusement. The basic idea was that there could be a public rebellion at such events as they saw huge gathering of Indians in a politically sensitive and critical time. These laws are still in effect in some states and are yet to be repealed or revised.

Contribution of Entertainment Tax in India

The states have started to generate higher incomes after the Paid Television Services began in India. At present there are some other sources through which state governments get their income tax related income:

- Broadcasting services
- Pay TV services
- DTH services
- Cable services

Entertainment tax Rates in India:

State	Entertainment tax levied on gross ticket value
Maharashtra	45.00%
West Bengal	30.00%
Gujrat	20.00%
Assam	15% for the tickets worth than less INR 20 and 20% for tickets worth more than 20 rupees
Delhi	20.00%
Orissa	25.00%
Uttar Pradesh	60.00%
Bihar	50.00%
Punjab	0.00%
Jharkhand	110.00
Haryana	30.00
Tamil Nadu	15% tamil language films are exempted from entertainment taxes.
Andhra Pradesh	20% in case of Telugu films the applicable rate is 15%
Kerala	30.00%
Jammu & Kashmir	0.00%
Rajasthan	0.00%
Himachal Pradesh	0.00%
Madhya Pradesh	20.00%

The following entertainment tax rates in the various states across India:

Implementation of Entertainment Tax in India

In India the aspect of entertainment is an intrinsic part of several transactions and services - this is done in such a way that the matter cannot be separated from the service or transaction itself.

Entertainment Tax in India - Collecting Authorities

In India, state governments are primarily responsible for collecting the entertainment taxes. However, the union government can also collect these taxes on the basis of the type of transaction.

The basic financial principle, which separates the entertainment taxes to be collected by the union government and ones under the jurisdiction of the state government, is mentioned in the Article 246 of the Indian onstitution. This part also highlights the entertainment taxes that can be collected by the union governments and the states.

Non- Tax revenue

The revenue obtained by the government from sources other than tax is called Non-taxes Revenue. The sources of non-taxes revenue are:-

1. Fees

Fees are another important source of revenue for the government. A fee is charged by public authorities for rendering a service to the citizens. Unlike tax there is no compulsion involved in case of fees. The government provides certain service and charges certain fees for them. For example: Fees are charged for issuing of passports, driving licenses, visit for any public park like national park

2. Fines and penalties

Fines and penalties are imposed as a form of punishment for breach of law or non fulfilment or certain condition or for failure to observe some regulations like taxes fines are compulsory payments without quid pro quo. But while taxes are generally imposed to collect revenue. Fines are imposed as a form of punishment or to prevent people from breaking law. They are not expected to be a major source of revenue to the government.

3. Surplus from Public Enterprise

The government also gets revenue by way of surplus from public enterprise. In India the government has set up several public sector enterprise to provide public goods and service. Some of the public sector enterprises do make a good amount of profits. The profits or dividends which the government gets can be utilized for public expenditure. There is some sort of quid-pro-quo in the case of surplus from public enterprise. This is because, the public gets goods and services and the government gets prices and consequently profits from selling such goods and services.

4. Special assessment of betterment levy

It is a kind of special charge levied on certain members of the community who are beneficiaries of certain government activities or public projects. For example, due to Public Park in a locality or due to construction of a road people in that locality may experience an appreciation in the value of their property or land. Thus due to public expenditure, some people may experience unearned increments in their asset holding. Betterment levy is like a tax because it is a compulsory payment. But unlike a tax, in case of betterment levy there is some element of quid pro quo.

5. Grants and gifts

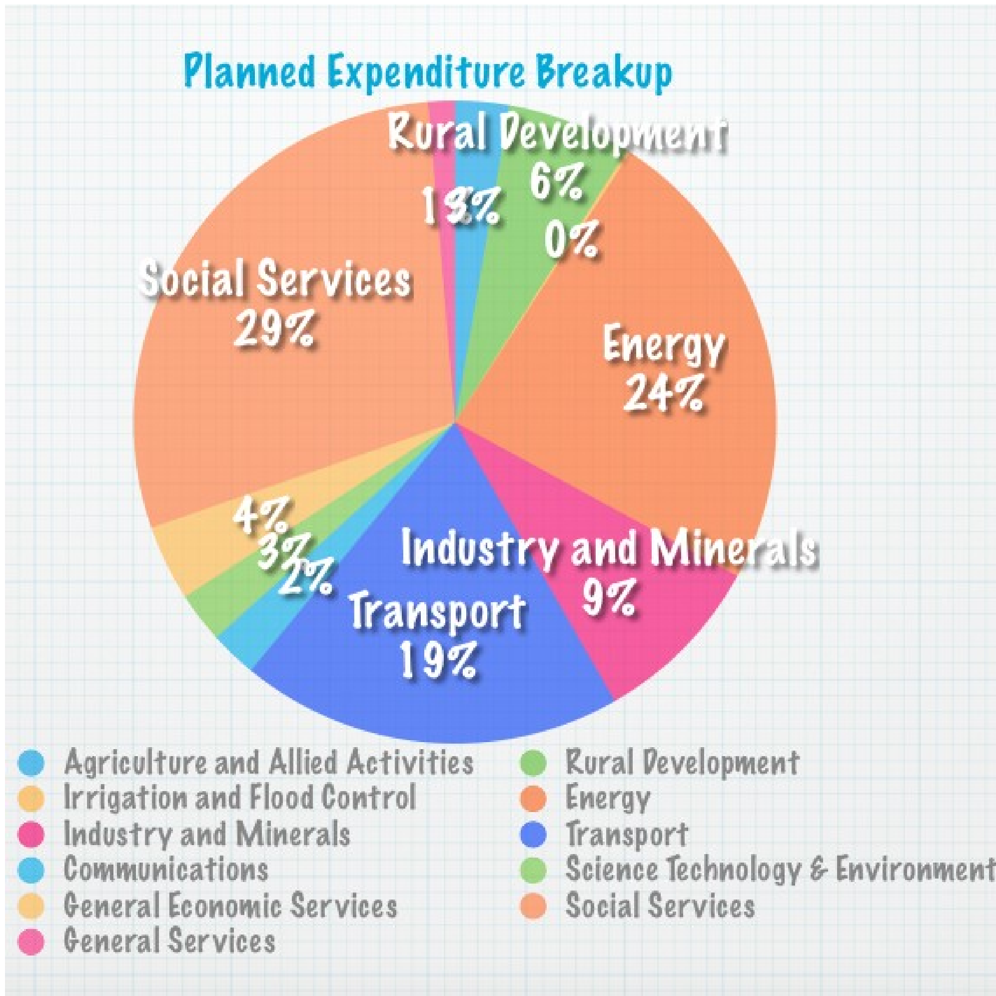
Gifts are voluntary contributions by individuals or institutions to the government. Gifts are significant source or revenue during war and emergency. A grant from one government to another is an important source of revenue in the modern days. The government at the centre provides grants to state government and the state government provide grants to the local government to carry out their functions. Grants from foreign countries are known as foreign Aid. Developing countries receive military aid, food technological aid, etc. from developed countries.

Where does the government spend the collection of money through taxation

Earlier in the week I looked at how the government raises money, and in this post I'm going to look at a few charts on how the government spends its money. There are two heads of government spending - Non Plan Expenditure and Plan Expenditure. Non Plan Expenditure is money that's spent on sustaining the country like defense, postal deficit, subsidies etc. and Plan Expenditure is the money that is spent on improving the country like the money spent on dams, roads etc.

But if the government spends so much on sustaining us - where does that money go?

Let's move on to plan spending. Here is a pie chart with the break up on the plan spending.



Planned Exp Breakup

The big spend here is Social Services and that comprises of a lot of items under broad heads like Education, Health, Housing, Art and Culture, Water Supply etc.

Agriculture and Allied Activities	17692.37
Rural Development	40763.45
Irrigation and Flood control	1275.00
Energy	154841.94
Industry and Minerals	57226.76
Transport	125357.06
Communications	15411.38
Science Technology & Environment	16597.65
General Economic Services	247770.28
Social service	188871.69
General Service	8700.67
Grand total	651509.25

Here are the absolute numbers.

I think perhaps the biggest thing to take away from this post is how nothing is free and how money that's used to subsidize oil has to be later borrowed which then accrues interest on it and then paying that interest eats up into money that you could use to finance growth.

CAPTER-7

Advantages and Disadvantages of Taxation to Redistribute Income

Taxation is a tool commonly used by government as a means of redistributing income amongst its citizens. In some instances, taxation can have a positive effect on the redistribution of income, other times, it can do more harm than good.

Taxation helps greatly in the redistribution of income as it gives the government funds which they can use to fund public services. In countries that have solid taxation systems, revenue from taxes will be great. The more revenue there is coming from taxes, the more money there will be left over for the government to provide public services to its citizens. Without the tax revenue that taxation offers, services such as protection from national police, provision of a transportation infrastructure, social security services, etc,. Social security services like welfare check programs help spread the wealth around a nation. The poor who don't have enough to live properly can apply for these welfare programs; they will receive checks funded by the taxes that individuals in higher income brackets pay.

On the other hand, there are also several disadvantages of using taxation to redistributing income. The main problem of using taxation to redistribute income is the possibility of ridiculously high effective tax rates. Though one might think that high effective tax rates would equate to more tax revenue, a high tax rate would give citizens a disincentive to work. People will start to wonder if it's worth putting so much effort into a job only to later realize that a large chunk of what they earn will be taken from them and given to the government.

One of the most commonly discussed issues in economics is how tax rates relate to economic growth. Advocates of tax cuts claim that a reduction in the tax rate will lead to increased economic growth and prosperity. Others claim that if we reduce taxes, almost all of the

benefits will go to the rich, as those are the ones who pay the most taxes. What does economic theory suggest about the relationship between economic growth and taxation.

Income Taxes and Extreme Cases

In studying economic policies, it is always useful to study extreme cases. Extreme cases are situations such as "What if we had a 100% income tax rate?", or "What if we raised the minimum wage to $50.00 an hour? While wholly unrealistic, they do give very stark examples of what direction key economic variables will move when we change a government policy.

First suppose that we lived in a society without taxation. We'll worry about how the government finances its programs later on, but for now we'll assume that they have enough money to finance all the programs we have today. If there are no taxes, then the government does not earn any income from taxation and citizens do not spend any time worrying about how to evade taxes. If someone has a wage of $10.00 an hour, then they get to keep that $10.00. If such a society were possible, we can see that people would be quite productive as any income they earn, they keep. Now consider the opposing case. Taxes are now set to be 100% of income. Any cent you earn goes to the government. It may seem that the government would earn a lot of money this way, but that's not likely to happen. If I don't get to keep anything out of what I earn, why would I go to work? I'd rather spend my time reading or playing baseball. In fact, going to work would risk my ability to survive. I'd be much better off spending my time trying to come up with ways to get the things I need without giving them to the government. I'd spend a lot of my time trying to grow food in a hidden garden and bartering with others for the things I need to survive. I wouldn't spend any time working for a company if I didn't get anything from it. Society as a whole would not be very productive if everybody spent a large portion of their time trying to evade taxes. The government would earn very little income from taxation, as very few people would go to work if they did not earn an income from it. While these are extreme cases, they do illustrate the effect of taxes and they are useful guides of what happens at other tax rates. A 99% tax rate is awfully like a 100% tax rate, and if you ignore collection costs, having a 2% tax rate is not much different from having no taxes at all. Go back to the person earning $10.00 an hour. Do you think he'll spend more time at work or less if his take home pay is $8.00 rather than $2.00? I'd bet you that at $2.00 he's not going to spend a lot of time at work and he is going to spend a lot of time trying to earn a living away from the prying eyes of government.

Taxes and Other Ways of Financing Government

In the case where government can finance spending outside of taxation, we see the following:

- Productivity declines as the tax rate increases, as people choose to work less. The higher the tax rate, the more time people spend evading taxes and the less time they spend on more productive activity. So the lower the tax rate, the higher the value of all the goods and services produced.

- Government tax revenue does not necessarily increase as the tax rate increases. The government will earn more tax income at 1% rate than at 0%, but they will not earn more at 100% than they will at 10%, due to the disincentives high tax rates cause. Thus there is a peak tax rate where government revenue is highest. The relationship between income tax rates and government revenue can be graphed on something called a Laffer Curve. Of course, government programs are not self-financing. We'll examine the effect of government spending in the next section.

Case Study

VODAFONE V/S INCOME TAX AUTHORITY OF INDIA – A PANDORA'S BOX

ABSTRACT

The case examines one of the largest merger and acquisition deals in India, how, Vodafone, oneof the world's largest mobile telecommunications company gained control over Indian TelecomCompany Hutch Essar through intermediate companies situated in Mauritius and CaymanIslands. It discusses the rationale for Vodafone's acquisition of 67% stake in Hutch Essar andalso examines the acquisition route adopted by Vodafone in order to avoid payment of capitalgains tax to the extent of two billion dollars which was accrued to the Indian Tax Authorities.The company refused to pay the capital gains tax arguing that the transaction has taken placeoffshore and hence it is not due in India. The case critically examines the arguments and counterarguments of Vodafone and Indian Tax Authorities as to whether the tax is due to be paid in India or not. The purpose of this case study is to understand the tax laws of India which are applicable to such kind of transactions. The study of the case is done purely on the secondary data and it is analysed according to the sections and regulations laid down by the Indian Tax Act.The case also ponders over an important aspect of mergers and acquisitions, whether investment through tax havens routes are genuine or are resorted to avoid taxes in home jurisdictions. Thestudy is presented in a form of case to elaborate it further and to use it by the students as well as the academicians.

Keywords:

Mergers and Acquisition, Income Tax Act, Capital Gains, Withholding Tax, Tax Havens

VS

Introduction:

Vodafone Essar Limited, formerly known as Hutchison Essar is a telecom serviceprovider in India that covers twenty three telecom circles in India and is based in Mumbai.Vodafone holds sixty seven percentage stake in Vodafone Essar Limited and Essar holds the restthirty three percentage stake. It is the second largest mobile phone operator in terms of revenueafter Bharti Airtel, and third largest in terms of customers. It has around ten thousand employeesacross India. It has a subscriber base of approximately one hundred and six million andcommands a market share of twenty four percent in India.On February 11, 2007, Vodafone agreed to acquire the controlling interest of sixty seven percentage held by Li Ka Shing Holdings in Hutch-Essar for US$11.1 billion. The company was valued at USD 18.8 billion. The transaction closed on May 8, 2007. Despite the official name being Vodafone Essar, its products are simply branded 'Vodafone'. It offers both prepaid andpostpaid GSM cellular phone coverage throughout India.

Background:

Vodafone Group Plc:

Vodafone Group Plc incorporated in England is the world's leading mobile telecommunications company. It is world's second largest mobile operator in terms ofsubscribers and largest in terms of revenue. It has a significant presence in Europe, the Middle East, Africa, Asia Pacific and the United States through the Company's subsidiary undertakings, joint ventures, associated undertakings and investments. It has approximately 347 million customers as on 31 March 2010. Currently, India is the third largest market after Germany andthe United States for Vodafone. The Company's ordinary shares are listed on the London Stock Exchange and the Company's American Depositary Shares ('ADSs') are listed on the NASDAQ Stock Market. The Company had a total market capitalisation of approximately £71.2 billion at 12 November 2009.

Vodafone Group has entered into arrangements with network operators in countries where the Group does not hold an equity stake. Under the terms of these Partner Market Agreements, Vodafone and its partner operators co-operate in the marketing of global products and services with varying levels of brand association. This strategy enables Vodafone to implement services in new territories and to create additional value to their partners' customers and to Vodafone's travelling customers without the need for equity investment in these countries.Similar agreements also exist with a number of the Group's joint ventures, associatedundertakings and investments (the affiliates).

Hutchison Whampoa:

Hutchison Whampoa Limited (HWL) of Hong Kong is a Fortune 500 company and oneof the largest companies listed on the Hong Kong Stock Exchange. HWL is an international corporation formed in 1863 with a diverse array of holdings which includes the world's biggest port and telecommunication operations in 54 countries. WL reports turnover of approximately HKD301 billion (USD39 billion) for the year ended 31 December 2009. Hutchison deals in the st businesses of ports and related services, property and hotels, retail, energy, infrastructure, investments and telecommunications. It belongs to the Cheung Kong Group and employs around 2, 20,000 people worldwide Hutchison Whampoa Limited based in Hong Kong is among the largest companies listed on the main board of the Hong Kong Stock Exchange. Flagship companies include Hutchison Port Holdings, Hutchison Whampoa Properties, A S Watson, Cheung Kong Infrastructure and Hutchison Telecommunications International Ltd.

Essar Group:

The Essar Group is a multinational conglomerate corporation in the sectors of Steel, Energy, Power, Communications, Shipping Ports & Logistics as well as Construction headquartered at Mumbai, India. The Group's annual revenues were over USD 15 billion in Financial Year 2008-09. Essar began as a construction company in 1969 and diversified into manufacturing, services and retail. Essar is managed by Shri.Shashi Ruia, Chairman – Essar Group and Shri.Ravi Ruia, Vice Chairman Essar Group. Essar

has its foot print over Asia, Africa, Europe and the America, and employs more than 50,000 people across the globe.

Hutchison Essar:

Hutchison Essar Ltd. ("Hutch India"), a company incorporated in India in 1994, was a joint venture of the Hong Kong-based Hutchison Telecommunications International Ltd ("HutchHong Kong") and the India-based Essar Group. Hutch India was in the business of providing telecommunications service in India. Hutch Hong Kong held sixty seven percent of the shares of Hutch India through CGP Investments Holdings Ltd ("the Cayman Islands Special PurposeVehicle"), an SPV registered in Cayman Islands, and some other shareholders.

The Event:

Vodafone Holdings International ("Vodafone"), a Dutch company, purchased shares of a Cayman Company – CGP Investments (Holdings) Ltd from a foreign company Hutchinson Telecommunications International Limited – HTIL for a total consideration of $11.2 billion. CGP Investments in turn held 67% stake of an Indian Telecom company (Hutch Essar) through intermediate companies situated in Mauritius. The sale ultimately resulted in the ownership of Hutch Essar by Vodafone Holdings International. The Indian Foreign Investment Promotion Board (FIPB) approved the said transaction on the condition that Vodafone would comply with all Indian municipal laws. Pursuant to theconsent of Essar Group, a new joint venture called the Vodafone Essar Ltd. (the new name of Hutch Essar Ltd.) came into existence.As a result of this sale, capital gains, estimated at $ 2 billion, accrued to the Cayman Islands SPV. Considered from the point of view of jurisdictions, it is clear that the sale transaction took place between the Dutch SPV (owned by a UK group) and the Cayman Islands SPV (owned by a Hong Kong company). The ultimate effect however was the transfer of controlling shares of an Indian company. Since the deal was offshore, neither party thought it was taxable in India. But the tax department disagreed. It claimed that capital gains tax, most people paid on the transaction and that tax should have been deducted by Vodafone whilst paying Hutch.The Income Tax Department has claimed capital gains under Section 9(1) (i) of the Income Tax Act as it is of the view that the transaction involved transfer of an Indian Asset and that the profit made by HTIL from the sale of shares to Vodafone was generated in India. Therefore, Vodafone had an obligation to pay withholding tax in India before making payment of purchase price to HTIL. The matter went to court.

Arguments of Vodafone:

Vodafone argued that the transaction took place between offshore entities owned by itself and Hutchison and was outside India's jurisdiction and moreover the deal was not taxable in India as the funds were paid outside India for the purchase of shares in an offshore company.Vodafone's contention was that the provisions were not applicable as the

primary obligation to discharge the tax was with the payee i.e. HTIL. Moreover withholding tax provisions cannot have extra-territorial application and is applied to companies of Indian residence only.

Arguments of Tax Authority:

But the tax department seeks to show that since most of the assets were in India, the deal was liable to Indian capital gains tax. Hutch had sold Vodafone valuable rights - including tag along rights, management rights and the right to do business in India and that the offshore transaction had resulted in Vodafone having operational control over the Indian asset, which is the second largest telecom service provider in India. The taxman's argument was focused on proving that even though the Vodafone-Hutch deal was offshore, it was taxable as the underlying asset was in India and so it pointed out that The capital asset; that is the Hutch-Essar or now Vodafone-Essar joint venture is situated here and was central to the valuation of the offshore shares. It also argues that under Indian law, the buyer in a deal is required to withhold any capital gains tax liability and to pay it to the treasury.

Treatment of Capital Gains on extra territorial transaction:

The Indian Parliament, under the provisions of the Constitution, has the competence toenact a legislation having an extraterritorial application. But it is unsure whether the Income Tax Act has such powers. According to Section 9 of the Income Tax Act, where a non-resident earns any income by a transfer of capital asset in India (whether direct or indirect), the capital gains taxwould apply. But Section 9 does not state that the transfer of the capital asset can be direct or indirect. It is only income which can be direct or indirect. Pursuant to Section 195 of the Act, every person paying any sum, which is chargeable to tax in India to a non-resident, must deduct income tax at source at the time of payment or credit.This applies to both residents as well as non-residents.

Withholding Tax

Withholding tax is a Government requirement for the payer of an item of income to withhold or deduct tax from the payment, and pay that tax to the government. In most jurisdictions withholding tax applies to employment income. Many jurisdictions also require withholding tax on payments of interest or dividends. In most jurisdictions there are additional withholding tax obligations if the recipient of the income is resident in a different jurisdiction, and in those circumstances withholding tax sometimes applies to royalties, rent or even the sale of real estate. Governments use withholding tax as a means to combat tax evasion, and sometimes impose additional withholding tax requirements if the recipient has been delinquent in filing tax returns, or in industries where tax evasion is perceived to be common. Typically the withholding tax is treated as a payment on account of the recipient's final tax liability. It may be refunded if it is determined, when a tax return is filed, that the recipient's tax liability to the government which received the withholding tax is less than the tax withheld, or additional tax may be due if it is

determined that the recipient's tax liability is more than the withholding tax. In some cases the withholding tax is treated as discharging the recipient's taxliability, and no tax return or additional tax is required.

Stance in favour of Vodafone Essar:

- Since the transaction took place offshore, the Income Tax Act shall not be applicable.
- The transaction was transfer of shares between two entities and as such there was notransfer of capital asset.
- The stake changed hands through a subsidiary in Cayman Islands that held shares in Hutchison Essar, now called as Vodafone Essar, through arms in Mauritius and India.Apart from the transaction being offshore, India has a double taxation tax treaty with Mauritius.
- As per the treaty, investments made in India from Mauritius are not subject to tax. The current tax regime sheds light on indirect tax that clarifies stance unlike the direct code.

Stance in favour of Income Tax Department:

- The routing of the whole transaction between the parties through their subsidiaries in Mauritius and Cayman was with the intention to evade tax.
- As per a precedent set in the Samsung case, where the Karnataka High Court upheld the Department's view that tax must be deducted on all overseas payments, whether or not that income is taxable. But all Courts do not agree.

- The High Court observes that Vodafone be treated as an "Agent" of Hutch, a non-resident, under Section 163 of the Income Tax Act and the said taxes shall be recovered from Vodafone. According to Section 160(1) of the Act, "Agent" of the non-resident is 'representative assessee', and Section 161 discusses the liability of representative assessee. Section 163 defines agent to include a person who has business connection with non-resident.

- The transfer in the current transaction represents a transfer of beneficial interest in theshares of an Indian company and hence, any gain arising from it would attract tax inIndia.

Observations of the High Court:

- The Court inferred that the subject matter of the transaction between Vodafone and HTIL is nothing but transfer of interest, tangible and intangible, in Indian companies of theHutch Group, in favour of Vodafone and not just an acquisition of shares of CGPInvestments.

- Vodafone had failed to produce the original agreement between Hutchinson Telecommunications International Limited and Vodafone, which makes it difficult to understand the true nature of the transaction between the parties, which leaves scope forvarious assumptions.

- With the signing of the agreement by Vodafone in February 2007 to acquire the interests in India, a nexus to a source of income in India was clearly established, even before theactual payment in May 2007.

- Representations made before FIPB, shareholders, regulatory authorities in the UnitedStates and Hong Kong makes it clear that the Hutch Group was transferring its interest inthe Indian Company.

    - As there was admittedly a transfer of controlling interest in the Indian company, there was an "extinguishment of rights" and "relinquishment" by the transferor in the shares of the Indian company which constituted a "transfer".

- The shares in the Cayman Company were merely the mode or the vehicle to transfer the assets situated in India. The choice of the assessee in selecting a particular mode of transfer of such assets will not alter or determine the nature or character of the asset.

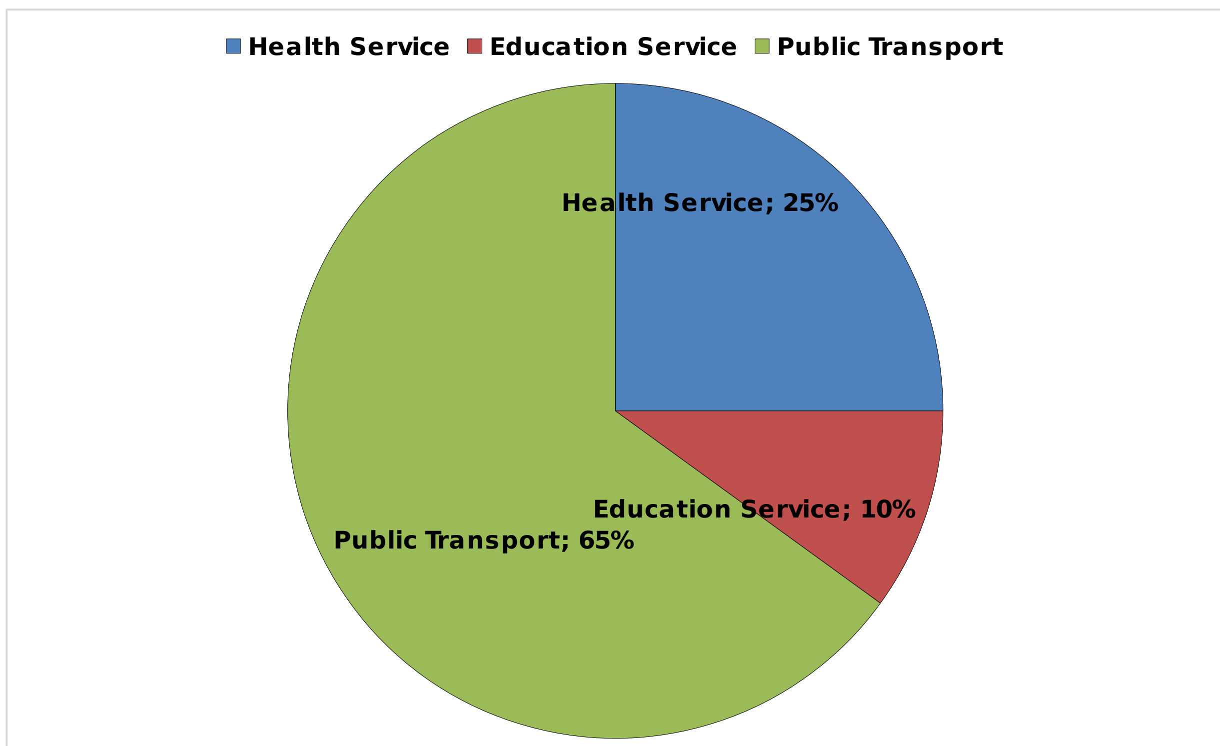
Conclusion

This transaction is one of the largest Mergers and Acquisition deals in India and the issuessurrounding this case can have wider ramifications on the Mergers and Acquisitions landscape in India. This case raises certain pertinent questions and shows the loopholes of the Indian Tax system like 1) how to access the impact on cross border transactions between two non-resident entities which have Indian assets and whether an Indian Company can be treated as 'agent' of the non-resident purchaser and held liable for deduction of tax. 2) Would there be an adverse effect on the foreign inflows where the foreign investors would think twice before investing in India ifthey are wary of the hassles involving such issues of tax, jurisdiction and deal structuring. These questions are required to be answered at the earliest as it may raises apprehensions in the minds of the foreign investors who would like to have a long term investment strategy for India. As a part of corporate strategy companies should give appropriate attention to use of jurisdiction with good treaty networks for implementing global investment structures. Clarity and consistency in disclosures assumes significance in the wake of regulatory compliances and hygienic corporate communications. It is also important that companies should be prudent enough to review and understand the shareholder agreements, references to key business rightsand its transferability.

Survey

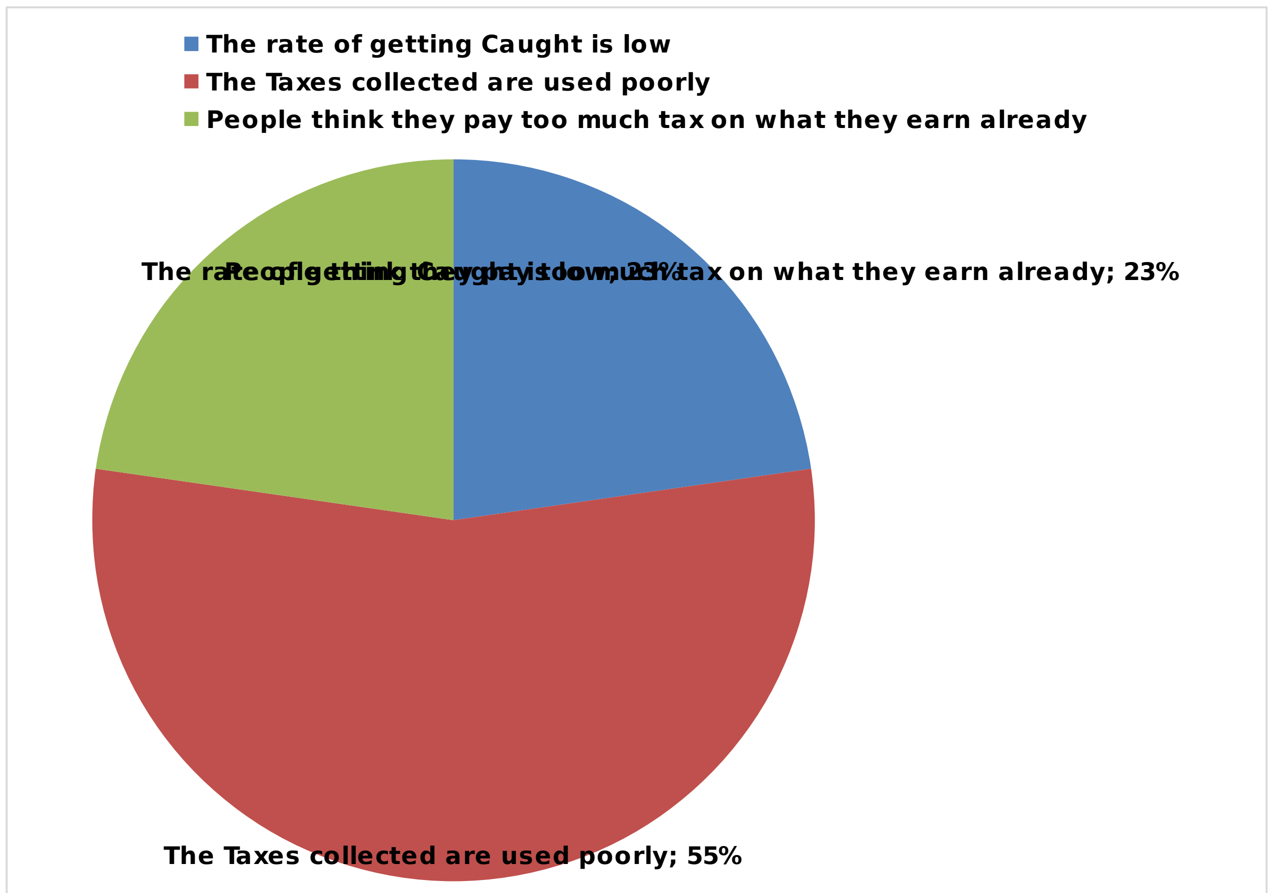
Parameters	Health Service	Education Service	Public Transport
Responses	05	02	13

1. What Are Your Taxes Used For?



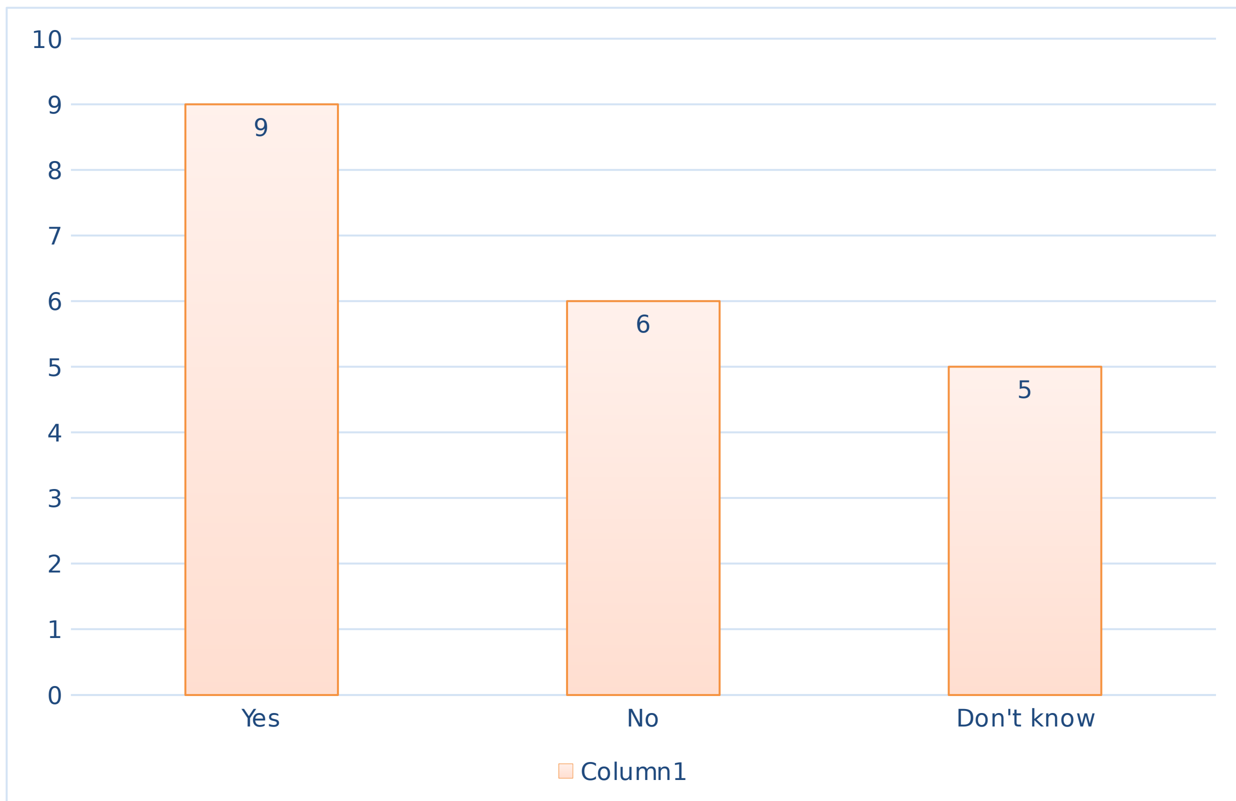
2. Why People do not pay their Taxes?

Parameters	The rate of getting Caught is low	The Taxes collected are used poorly	People think they pay too much tax on what they earn already
Responses	03	12	05



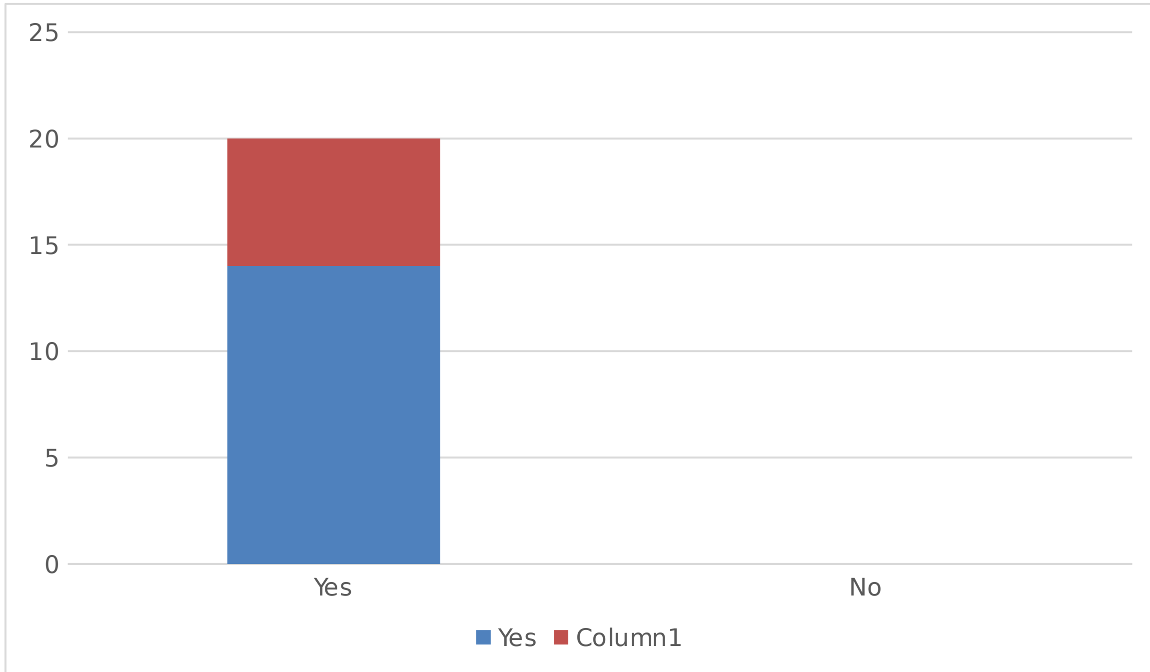
Parameters	Yes	No	Don’t know
Responses	09	06	05

3. revenue makes it easy for you to pay your taxes?



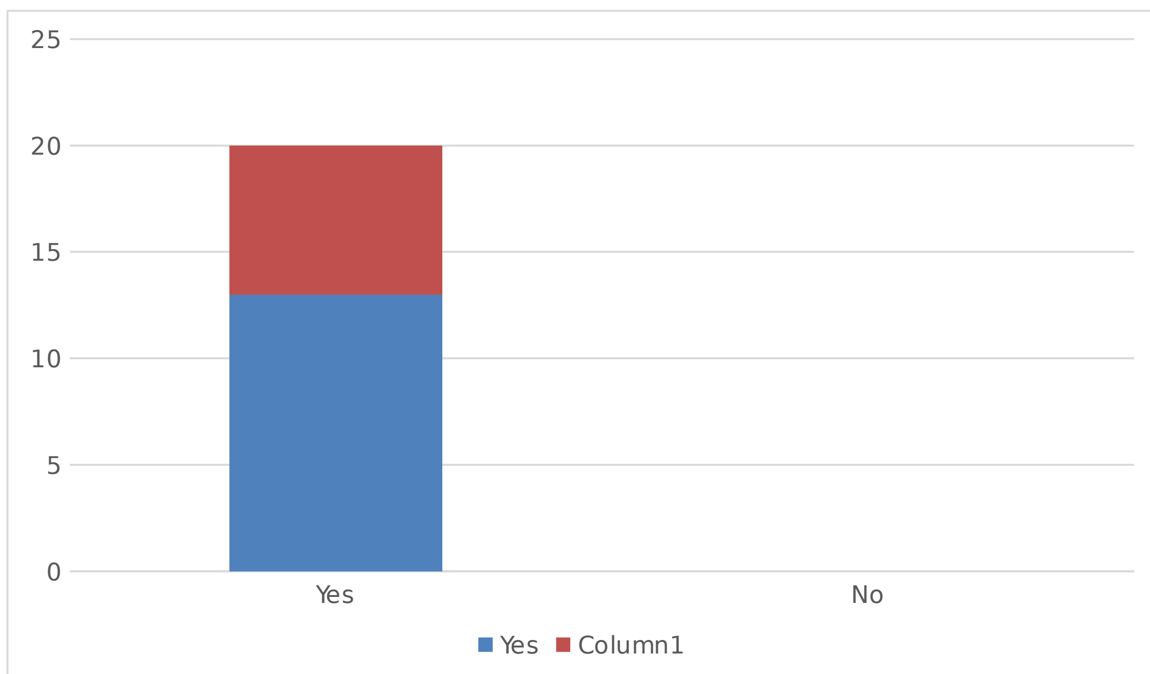
Parameters	Yes	No
Responses	14	06

4. The Taxes collected are used poorly?

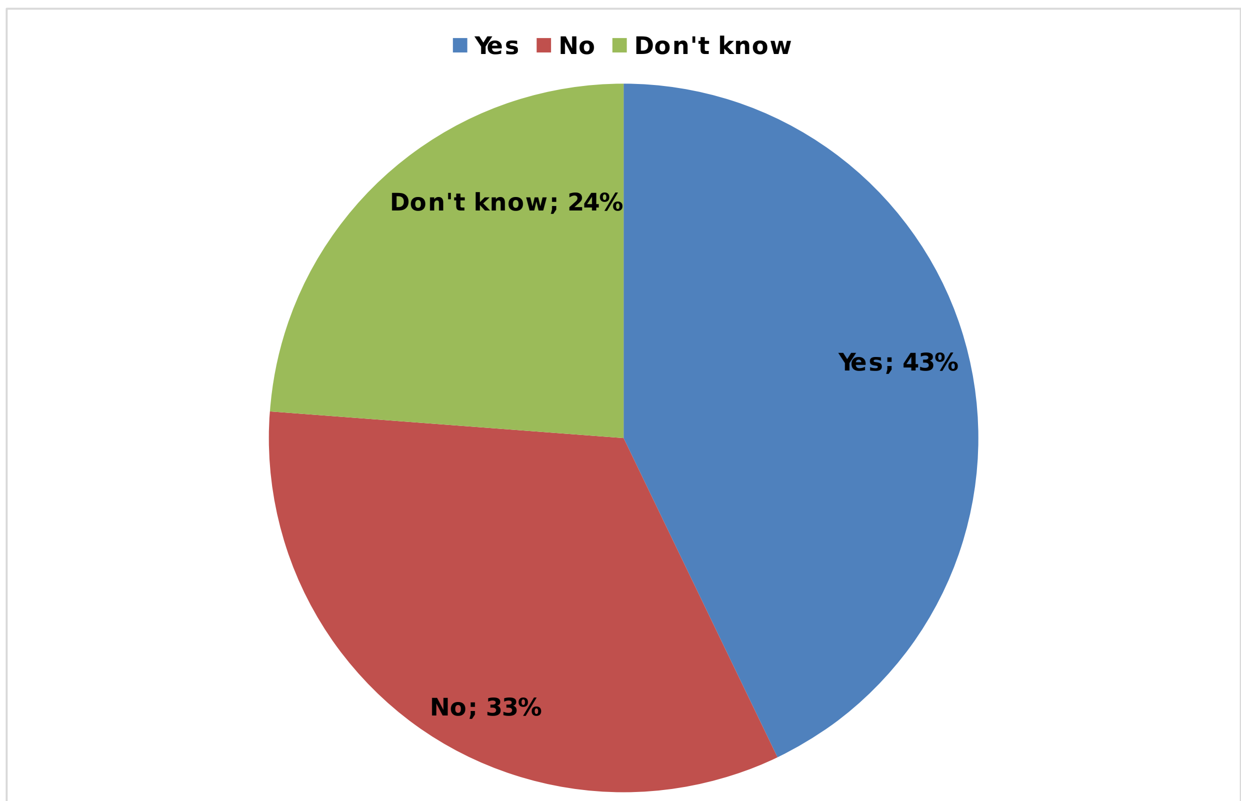


Parameters	Yes	No
Responses	13	07

5. Your Taxes are used to pay for Public services?



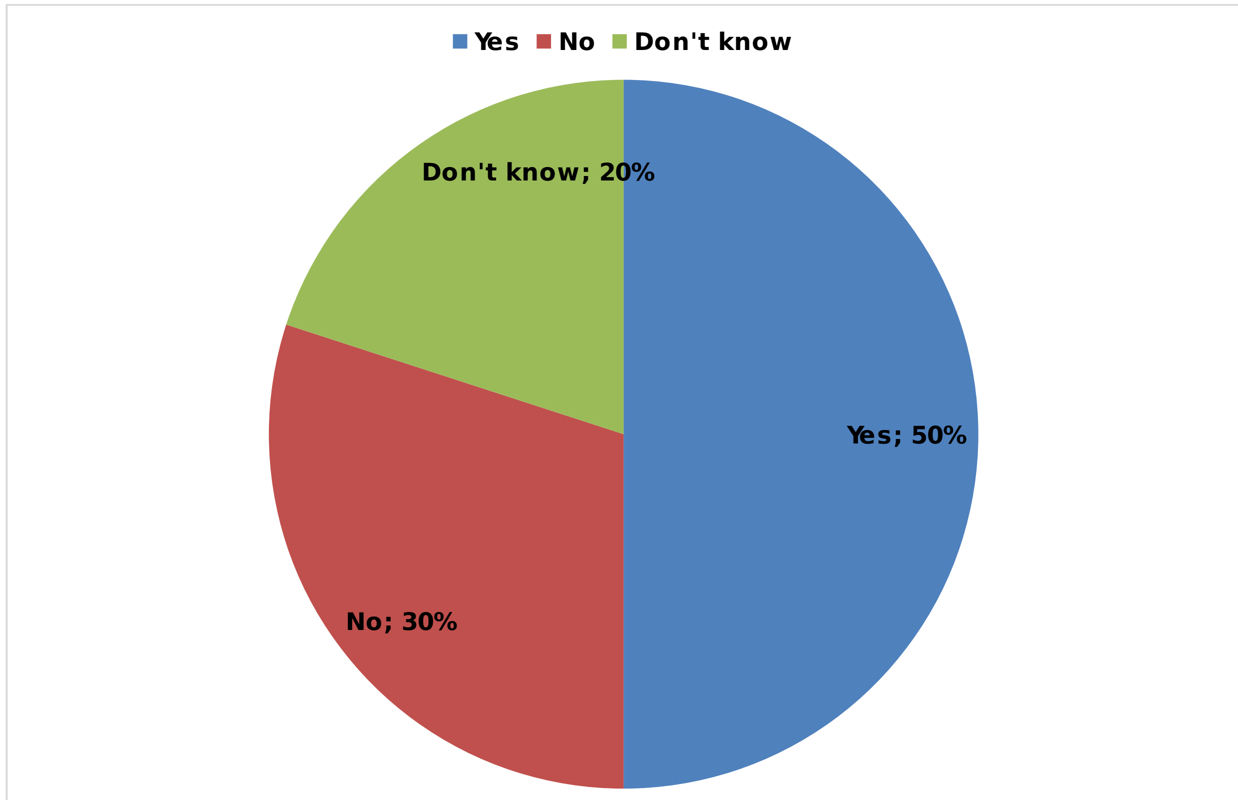
6. Revenue Online forms are easy to complete?



Parameters	Yes	No	Don't know
Parameters	Yes	No	Don't know
Responses	10	06	04

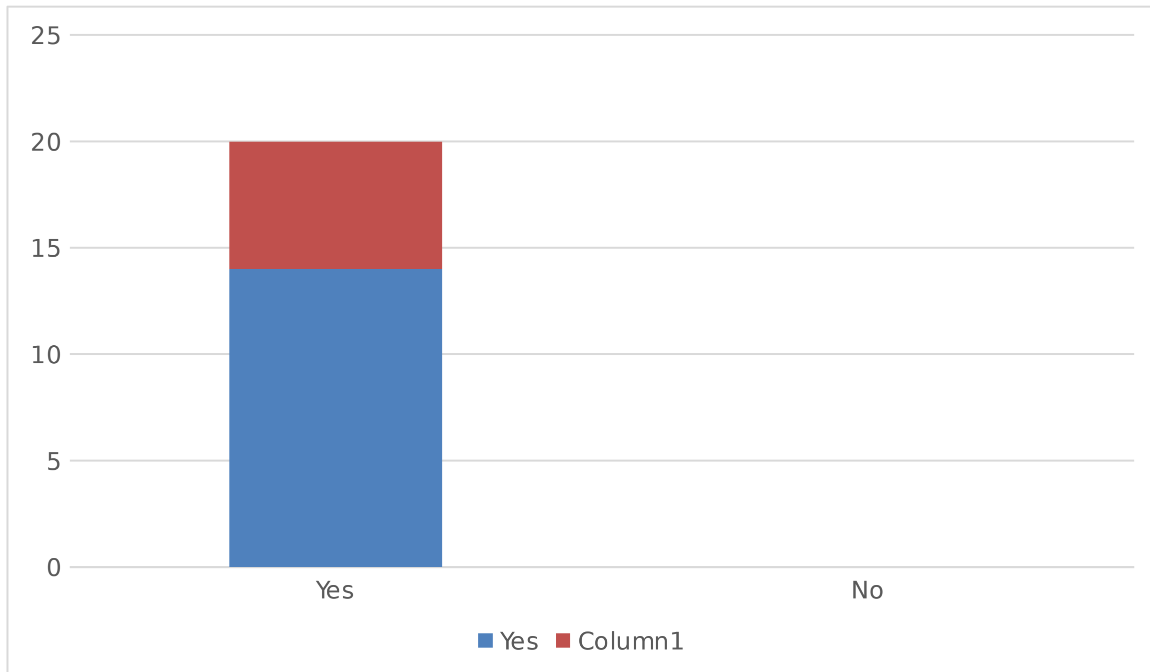
7. How well informed would you consider yourself to be regarding your task affairs and tax entitlement?

Parameters	Yes	No
Responses	14	06

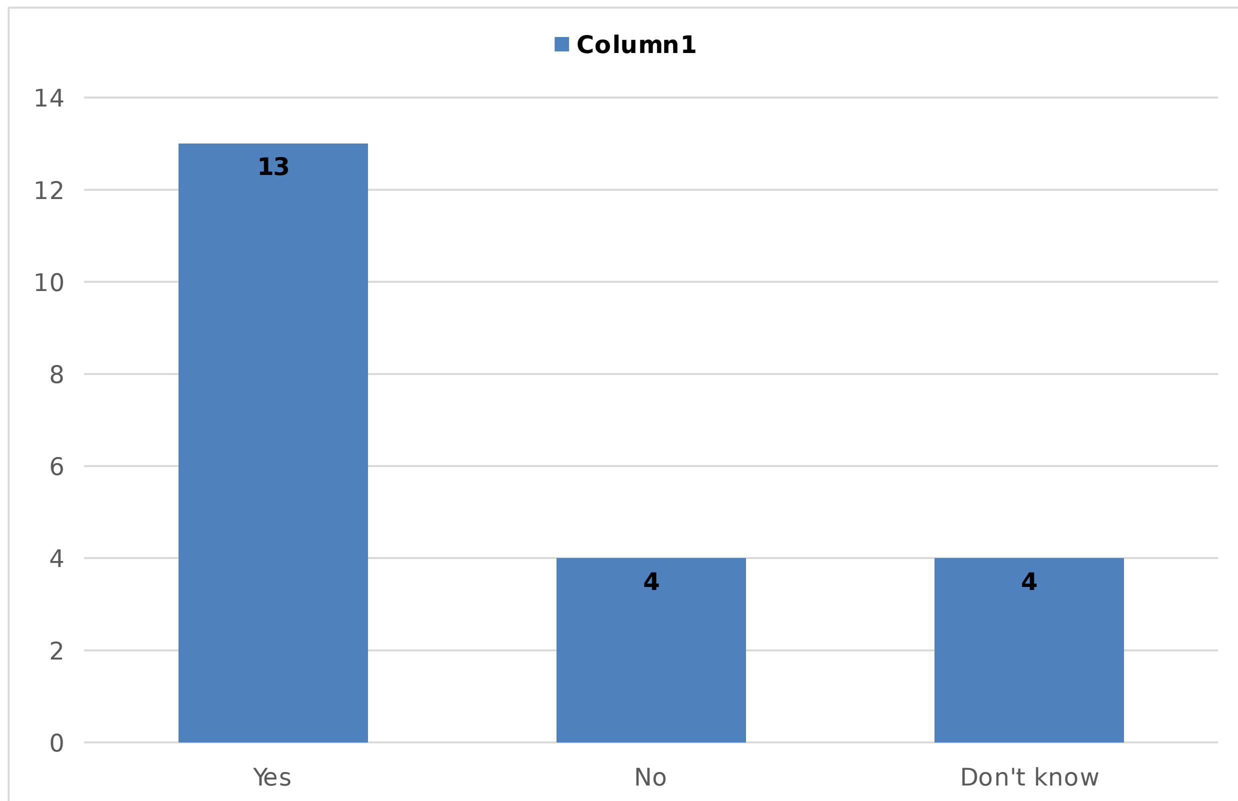


8. Not fully reporting all of you income to reduce the Amount of pay?

Parameters	Yes	No	Don’t know
Responses	13	04	03

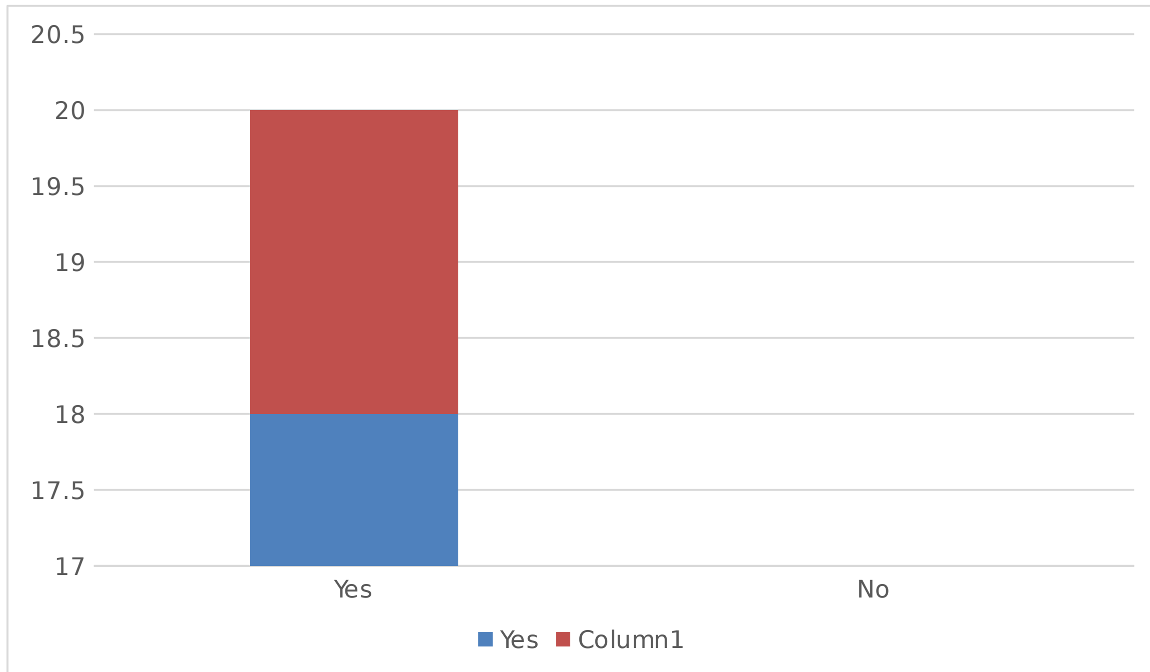


9. Few people report all of their income to revenue?



10. Tax paying is a Law?

Parameters	Yes	No
Responses	18	02



CONCLUSION

Taxation is a very important branch to study & understand the overall gamut of the Taxation system of India. In last 10-15 years, Indian taxation system has undergone tremendous reforms. The tax rates have been rationalized and tax laws have been simplified resulting in better compliance, ease of tax payment and better enforcement. The process of rationalization of tax administration is on-going in India. Since April 01, 2005, most of the State Governments in India have replaced sales tax with VAT. After conducting a comprehensive evaluation for this project, I immensely pleased in stating that a significant and innovative step has indeed been taken by the Central Government in coordination with and the State Governments to improve the efficiency and productivity of the tax systems prevailing in India. This pioneering move will not only aid in rendering satisfaction and economical growth but will also yield in establishing a healthy image of taxes and their derived benefits in the minds of the citizens. The first part of this project shows great potential and by far has been successful in fulfilling all the aspired objectives in the field of direct taxes. However, in the second part it indirect taxes are explained. It is strongly emphasizes upon the highlighted recommendations and focused aspects that may for the future positively render in establishing thorough professionalism and more stability. Significantly, it is further suggested to proceed with the commencement of both the parts of this project as this radical step to add value to the present taxation system and boost the economy thus introducing an era of change and advancement.

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