

Tax Hotline

May 02, 2008

ONE YEAR FURTHER RELIEF TO SOFTWARE UNITS, BUT NOTHING MORE!

India's Finance Minister P. Chidambaram ("**FM**") on Tuesday, April 29, 2008 proposed several changes to the Finance Bill 2008 ("**Finance Bill**") that was tabled before the parliament on February 29, 2008 earlier this year. One of the key changes to the Finance Bill 2008 is the proposed extension of tax holiday to units set up in Software Technology Parks, Hardware Technology Parks, Free Trade Zones, and 100% Export Oriented Units. These units are currently enjoying a tax holiday under Section 10A and 10B of the Income Tax Act, 1961 ("**ITA**"). However, the sunset clauses under sections 10A and 10B of the ITA stipulate 31 March 2009 as the date on which the exemptions will come to an end. The IT Industry had been putting forth various submissions before the Indian Government seeking an extension of the tax holiday especially in the wake of the strengthening rupee, and the corresponding declining export profits. The FM, while announcing the **Budget 2009** in February shattered the hopes of IT industry by not announcing any extension of the tax holidays currently available to these IT units. The FM has now extended this exemption available to the IT industry mentioned above for a further period of one year until 31 March, 2010.

In his speech before the Lok Sabha last Tuesday, the FM remarked that "**eventually, we would have to move towards a system of taxation where the exemptions are few, each exemption is reviewed periodically and each exemption comes to an end after a reasonable period of time**". The FM also said that the most appropriate occasion to announce a decision in this regard would have been Budget 2009-10. However as this budget may not be presented on time in February due to elections and with a view to avoid uncertainty as the days draws closer to 31 March 2009, the FM decided to make amendments to Section 10A and 10B as mentioned above.

ANALYSIS

The IT sector especially the small and medium industry has been under tremendous pressure due to rupee appreciation. In order to mitigate the reduction in profits as a result of appreciation in rupee the companies are resorting to several cost cutting measures. Parul Jain^[1] feels that "**Although the extension of the tax holiday has come in as a welcome relief to the IT industry, it is an interim relief and will leave the IT Industry vying for more next year. Further, the FM's speech gives out a possible indication that the FM has no intention of extending the tax holiday for a prolonged period as desired and hoped by the IT Industry. This could mean a difficult time for the IT Industry especially since a shift to Special Economic Zones which currently offer a fifteen year phased tax holiday to units set up therein, may not be permitted.**"

The FM has also indicated that his intention of moving towards an exemption free system of taxation would be mirrored in the new Income Tax Code, which is expected to be placed in the public domain for comments in the near future. However, in the meanwhile, the extension of the tax holiday by one year comes as a welcome relief.

- **International Tax Team**

[1] Parul Jain is a senior member of our taxteam

Sources:

1. Text of Further Proposed Amendments to Finance Bill 2008 from www.taxmann.net
2. Analysis of Further Proposed Amendments to Finance Bill 2008 from www.taxmann.net
3. Extract of the FM's speech on Finance Bill 2008 in Lok Sabha
4. The Economic Times April 30, 2008
5. The Hindu April 30, 2008
6. www.livemint.com.

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