FINAL REPORT

OF THE

EXPERT GROUP

ON

TAXATION OF SERVICES

DEPARTMENT OF REVENUE, MINISTRY OF FINANCE,
GOVERNMENT OF INDIA.
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01. EXECUTIVE SUMMARY:

01.1 The important objectives of reforms in regard to taxation of services inter-alia include broadening the tax base, simplifying the structure and streamlining and rationalizing the system to improve revenue productivity, ensure neutrality in domestic trade taxation, and hasten the evolution of a co-ordinated and harmonized consumption tax system in the country. At present, while the manufacturing sector with only 19 per cent contribution to GDP bears a disproportionate share of the burden of indirect taxation, the services sector with over 50 per cent of GDP contributes only marginally to taxation. The coverage of selective taxation of services is just about 5 per cent and almost 95 per cent of this sector remains outside the purview of taxation. In addition, some contribution is made when excisable goods are used as inputs in the production of services, but the amount of tax thus generated is not very significant.

01.2 Taxation of services should be structured as a simple, broad based, transparent levy with a low rate, initially. The tax system should be such that it does not lead to cascading and should eventually be integrated with the CENVAT to evolve a manufacturing stage Central value added tax (VAT). It is necessary to dispense with the present approach of selectively taxing services in favour of a general taxation of all traded services with minimum exemptions. However, in doing this, it is necessary to keep in view the socio-economic realities. All public services, services of meritorious nature, services with significant externalities and those in the unorganised sector may be kept outside the tax net. The tax rate should be low so as not to have an adverse impact on compliance as well as it does not come in the way of expanding the base to cover all services. The tax should promote voluntary compliance. We have, therefore, recommended the continuation of the tax at 5 per cent until the tax on services is coordinated with that on goods. Eventually, the tax on services may be integrated with those on goods to enable a manufacturing level VAT by 2004-05.

01.3 Keeping in view administrative feasibility and convenience, it is desirable to exempt all service providers up to a threshold of Rs. 10 lakh turnover per annum. For the present, the tax rate may be levied at 5 per cent, but input tax relief should be extended within the service sector. When the service tax is integrated with the CENVAT, a revenue-neutral uniform rate of tax will have to be determined for the total base of goods and services. As a measure of rationalization / simplification, it is also necessary to reconsider multiple taxation of certain services as the service tax will cover these bases as well, though this may lead to some revenue losses.

01.4 We recommend enactment of a self-contained code for administration of service tax in the interim period of its integration with CENVAT. Administration of a separate Service tax law with comprehensive coverage and an internal credit mechanism need a well-defined administrative arrangements under the CBEC with adequate budgetary provisions, high degree of financial autonomy and accountability. In order to promote voluntary tax compliance a computerized on-line web based tax administration system may be introduced and service tax administered as the first e-tax of the country. The administrative system in service tax should provide a model for computerized administration, filing of returns, information base and retrieval to other taxes.

01.5 Keeping the above norms in view, all traded services from the following sectors and allied services incidental thereto would attract 5 percent service tax levy. Rail / Road/ Water/ Air transport of goods and passengers, storage and warehousing, Post and telecommunications, Banking and financial services sector (excluding lending, borrowings and other financial intermediation services) construction / maintenance of buildings, road, rail beds, bridges, waterways, reservoirs hydroelectric projects, construction (non essential sector), Hotels and restaurants, Business Services (except IT Services/enabled services), Education Services (excluding education up to class twelve) Health and Medical Services (excluding essential medical and family welfare services) and Media Services. It is difficult to precisely estimate the revenue gain when tax base is widened as above, but it is expected to be significant.

01.6 For evolution of a comprehensive destination based consumption type VAT at the state level, sharing of power to levy tax on services with the states is desirable. This may require an amendment to the Constitution. However, before sharing these powers, the Central Government should ensure that the states are committed to uniformly implement state level VAT on goods and services at a standard rate without any discrimination.

01.7 Accordingly, we have made the following specific recommendations.

(i) The **service sector should be comprehensively covered** under the Service Tax net. However, services relating to public utilities, sovereign functions of the State, essential health and education services could be excluded from the tax net by incorporating a **well-defined negative list.** (para 06.1)

(ii) The unorganised sector and small service providers should be kept out of the purview of this tax by prescribing a **threshold exemption** limit of annual turnover up to **Rs.10 lakhs.** (para 06.2)

(iii) **Certain services,** which are developmental in nature or cater to primarily lower strata of the society, **may be exempted for a limited period.** (para 06.2)

(iv) The tax on services should be eventually integrated with Central Excise duties on goods to evolve into a **comprehensive CENVAT on goods and services by 2004-05.** (para 06.6)

(v) In the meantime, the **input credits should be immediately allowed within the service sector.** Inter-sectoral credits between goods and services could be extended along with integration into CENVAT.(para 06.3)

(vi) **The rate of service tax** for the present could be retained at the present moderate rate of **5 percent.** (para 06.4)

(vii) A **separate, self-contained enactment on service tax** should be legislated to administer the service tax. (para 06.5)

(viii) An **improved administrative arrangement** with increased financial autonomy is important for successful implementation of this tax. (para 06.8)

(ix) In order to facilitate voluntary tax compliance and to cut down taxpayer inconveniences the service tax should be administered as the **first e-tax of the country** with self assessment and risk based audit and online web based connectivity with assessees. (paras 06.6.4, 06.7 & 06.8.6)

(x) The Central Government should consider **sharing of powers to tax services with the states** once the latter are committed to uniformly introduce a comprehensive destination based VAT. (para 06.10)

(xi) A well-orchestrated **publicity campaign for taxpayer education** is essential for smooth implementation of our recommendations. (para 06.9)

02. INTRODUCTION:

02.1 The share of service sector in the Indian economy has increased significantly over the years. The growth of income from the services sector which was just about 2 percent per annum in the 1980s, accelerated dramatically to an average of 8.2 percent in the 1990s. As the services sector emerged as the fastest growing sector in Indian economy, much faster than both primary and secondary sectors, it altered the basic structure of Indian economy. Thus, the services sector has emerged as the largest contributor to the GDP in the country and it presently contributes about 52 percent of GDP.

02.2 While the largest component of GDP in the country comes from the services sector, its contribution to the exchequer has been abysmal and not at all commensurate with its predominant position in the economy. Services sector is the largest contributor to both production and consumption in the economy. With the increase in incomes, increasing proportion of such incomes is spent on the consumption of services. While the goods produced and consumed are subject to multiple levies such as union excise duties, sales tax, entry tax or octroi etc. by central, state and local governments, most of the services are not directly subject to taxation. Since 1994, the central government has extended the tax to a few selected services by invoking residuary powers under Entry 97 of the Central list in the seventh schedule of the Constitution. At present, very few services are subject to taxation. In respect of others, the tax is payable on services only when they enter into the production of goods and the latter is subject to taxation. However, this tax incidence constitutes a negligible portion of total tax revenue. Thus, production and consumption of services, which constitute a large and growing proportion of the economy contribute very little by way of taxation. Extending the tax to the services sector is imperative not only to ensure neutrality and horizontal equity in taxation but also to broaden the tax base and improve revenue productivity of the tax system.

02.3 As mentioned above, the manufacturing sector bears disproportionately large burden of indirect taxation and this lopsided approach to taxation causes serious distortions and inequity in the tax system. Extension of service tax is particularly important from the viewpoint of neutrality in taxation. Besides, broadening the tax base to include services would require levying taxes at lower rates to generate the required revenue receipts. Such lower marginal tax rates cause lesser relative price distortions between goods and services.

02.4 The most important factor warranting the levy of taxation on services is the need to evolve a coordinated system of domestic trade taxes both at central and state levels. Services enter into the production of commodities and vice versa and in order to relieve taxes on inputs, be they on goods or services, it is important to levy the tax on both goods and services. Over the years, by extending input credit schemes, union excise duty has almost been transformed into manufacturing stage VAT at Central level. However, services have remained outside this system and therefore, it has not been possible to provide credit for all input taxes, both explicit or implicit. Therefore, it is necessary to evolve a suitable mechanism to provide input tax relief on the taxes paid on services so that a coordinated system of taxation on goods and services could be developed.

02.5 The Tax Reforms Committee headed by Dr. Raja J. Chelliah recommended the imposition of tax on select services. Based on these recommendations, the Central Government made a modest beginning by imposing service tax on 3 services, i.e., telephones, non-life insurance, and stockbrokers, in 1994. Over the years, the scope of the service tax has been expanded to cover 26 services. In the budget proposals for 2001-2002, the Government has proposed the levy of service tax on 14 more services, thereby increasing the tax net to cover 40 services. The service tax, which is presently levied at the rate of 5 percent, is likely to contribute approximately Rs.2200 crores in the year 2000-2001, as compared to Rs.2072 crores in 1999-2000.

02.6 The limited experience gained in taxing the services on a selective basis has raised some important issues. The most important of them relates to the basic approach to taxing services. The selective approach to taxation, which has been followed till now, has given rise to many administrative problems arising from selectivity including inadequate coverage and increased litigation. Further, in accordance with the medium term policy objective of the Government of evolving a manufacturing stage value added tax in respect of goods and services at central level, it is necessary to adopt a more general approach.

02.7 The second issue relates to manner of imposition of tax so that the consumer choice is not distorted and the consumption pattern of taxable services is maintained even while realising their due tax potential. This underlines the need for non-discriminatory treatment of goods and services for taxation purposes. The best way to develop a neutral tax system is to levy the value added tax (VAT). It is therefore necessary to prepare a roadmap for evolution of manufacturing stage VAT at central level by developing a coordinated system of taxing goods and services. However, in evolving efficient domestic trade tax system in the country, it is important to take into account socio-economic realities and developmental considerations. This implies that services, which constitute the basic administrative fabric, those that are meritorious, and with significant externalities and those essential for human development and physical progress will have to be identified for exemption. Administrative considerations also necessitate exemption of services in the unorganised sector and small service providers from the purview of taxation. This is necessary also to avoid harassment. Exclusion of such segments from the scope of the tax without compromising on the fundamental approach of expanding the tax base is also an important issue.

02.8 The central Government is simplifying and rationalisating the rate structure of excise duties with a view to converting it into a VAT by providing input tax credit. It is advisable to follow the same approach on the service tax also. Thus, it is appropriate to continue with the present system of single rate of tax on services even after the tax base is expanded to cover all services. Simplicity in the rate structure is important from the viewpoint of administration and compliance and eventual integration of service tax with CENVAT on goods.

02.9 Setting up of an effective and progressive tax administration set up is vital for ensuring better tax compliance. The service tax being an indirect levy, is administered by the Central Board of Excise and Customs. The internal structure of this tax machinery would have to be so organized as to effectively handle the needs of service sector also. A computerized information based tax administration system would go a long way in increasing the efficiency while at the same time reducing the cost of collection.

02.10 It is also important to have a well-orchestrated publicity campaign for the tax. This tax should be seen not as an addition to the existing multiple levies, but as a better and more scientific substitute to them. It should be seen by the public as a tool to rationalise the existing domestic trade tax system – to broaden the base, reduce the rate and more importantly, relieve the taxes paid on inputs and capital goods. Unless the tax is extended to services, the cascading caused by the input taxes implicit in the value of goods and services cannot be relieved. Therefore, from the viewpoint of inter-alia production efficiency, minimising cascading and to zero-rate the taxes on exports, it is essential to levy the tax on services. It would also lead to improved competitiveness in economy and expansion in domestic and international trade. It is important to make the public to understand these arguments so that they appreciate the basic rationale for extention in scope of the tax. It is, therefore, necessary to launch an ongoing publicity drive through the audio/visual and print media highlighting the economic necessity and rationale of taxation of services and its eventual integration with the union excise duties.

03. CONSTITUTION OF THE EXPERT GROUP:

03.1 The Hon'ble Finance Minister, while presenting the Union Budget for the financial year 2000-2001, had stated in the Lok Sabha that the Government had decided to set up an Expert Group to go into all aspects relating to taxation of services. In accordance with the announcement made by the Finance Minister, the Government of India constituted a seven member Expert Group, vide resolution dt. 27.06.2000 (F.No.168/68/99-TC).

03.2 Subsequent to the issue of aforesaid resolution, Prof. Indira Rajaraman, one of the members, expressed her inability to join the Expert Group. Thereafter, the Expert Group in its first meeting held on 24.07.2000, decided to co-opt Dr. M.G.Venugopalan, Director General, Service Tax, Mumbai, as a member in view of his wide experience in the administration of the indirect taxes and the service tax in particular.

03.3 The final composition of the Expert Group is as follows:

01.	Dr. M.Govinda Rao, Director Institute of Social & Economic Change	- Chairman
02.	Shri B.C.Rastogi, Former Chairman, Central Board of Excise & Customs	- Member
03.	Shri D.B.Lal, Former Member, Central Board of Direct Taxes	- Member
04.	Shri Ashok Wadhwa Tax Expert & Consultant	- Member
05.	Dr. Arvind Virmani, Senior Economic Advisor, Ministry of Finance	- Member
06.	Shri Sukumar Shankar, Member (Budget), Central Board of Excise & Customs	- Member Secretary
07.	Dr. M. G. Venugopalan, Director General, Service Tax.	- Member

03.4 The terms of reference of the Expert Group are:

(i) To examine the existing structure of service tax and to make recommendations on extending the tax base in the areas of services and the timing thereof.

(ii) To examine the existing procedure for collection of service tax, and to make recommendations as may be considered necessary for making it more effective, to augment voluntary compliance, and to reduce compliance cost.

(iii) To make recommendations on any other matter related to the above points or incidental thereto.

Subsequently, vide letter dt. 19.01.2001 (F.No.168/68/99-TC (Pt.)), the Government desired that the Expert Group may also examine the likely impact of wider coverage/sharing of services under service tax on taxation base of the states.

03.5 The Expert Group was required to submit an interim report by 31.10.2000 and the final report by 31.12.2000. The interim report was submitted on 23.11.2000. Subsequently, the Government was requested to extend the time for submission of final report upto 31.03.2001. This final report is being submitted accordingly.

04. PROCEEDINGS OF THE EXPERT GROUP:

04.1 The Expert Group held 10 meetings from July 2000 to March 2001. The deliberations were inter-alia devoted to arrive at working solutions to the issues placed before it by the Government.

04.2 In order to make the recommendations more broad based, the Expert Group interacted with various authorities in the Government and members of trade and industry. Interactive sessions were held with Shri P.G.Mankad, the then Finance Secretary, Shri B.P.Verma, Chairman, Central Board of Excise and Customs and Dr. Parthasarathi Shome, Chairman, Advisory Group on Tax Policy & Tax Administration, appointed by the Planning Commission. The Chairman and Member–Secretary had separate discussions with Dr. S. Narayan, Revenue Secretary and Prof. Raja J. Chelliah, Chairman, Madras School of Economics and former Chairman of Tax Reforms Committee. The representatives of various trade bodies like FICCI, ASSOCHAM, PHD Chamber of Commerce & Industry, All India Motor Transport Congress, Institute of Chartered Accountants (Western India Regional Council), Mumbai Chartered Accountants Society and Bombay Custom House Agents' Association made presentations before the Expert Group. The Confederation of Indian Industries (CII) chose not to make a separate presentation, as their tax panel head Shri Ashok Wadhwa is a member of the Expert Group. A delegation of the officers of Indian Post & Telecom Accounts & Finance Services (IP&TAFS) also made a presentation before the Expert Group requesting for being redeployed for collection of service tax from the telecom sector.

04.3 In order to ascertain the views of the trade and service providers in all sectors regarding the scope of its work, the Expert Group circulated a questionnaire to a number of trade bodies. A copy of questionnaire was also forwarded to all the State Governments, Chairman, Railway Board, Secretary, Ministry of Civil Aviation and the Director General of Health Services. Further, a number of noted economists and public finance experts were requested to forward their views. Though the responses were expected to be received by 31.08.2000, these continued to be received till December, 2000. A brief survey of responses received is presented separately in this report.

04.4 The Expert Group took the assistance of M/s. Arthur Andersen for carrying out various studies. These studies pertained to the following:

(i) Ascertaining the service tax law, practice and procedures followed in various countries such as Canada, Australia, Malaysia, Singapore, China, United Kingdom, Netherlands, and Philippines.
(ii) Ascertaining the assessment and audit procedures regarding service tax in the said countries.

(iii) Carrying out a detailed analysis of the service sector to ascertain the scope for expanding the tax base, revenue potential and scale of exemptions.

04.5 The Fiscal and Monetary Policy Division of the Reserve Bank of India was also requested to comment on the feasibility and the scope of taxing the services in the financial sector. The RBI was further requested to offer their views on the imposition of service tax on services relating to foreign exchange transactions. The report of the RBI was received in November, 2000. Additionally, M/s. Arthur Andersen also carried out a detailed study to estimate the revenue potential of the banking and financial services sector. The views emanating from these studies have been appropriately considered while finalising our recommendations.

05. APPROACH TO EXPANDING THE SERVICE TAX BASE:

05.1 Fiscal Situation in India and need for expansion of service tax base:

05.1.1 The principal motivation for expanding the tax base and improving the revenue productivity of the system is to correct the unsustainable fiscal situation the country is presently faced with. Despite almost a decade of fiscal adjustment, the situation is far from being satisfactory and fiscal consolidation is yet to be achieved. Increasing revenue deficits of both central and state governments caused significant decline in public savings. Public savings as a ratio of GDP declined sharply from 2 per cent in 1995-96 to -1.2 per cent in 2000-01. The revenue deficit of the central government alone increased from 2.5 per cent to 3.6 per cent during this period. Similarly, the fiscal deficit-GDP ratio of the central government increased from 4.2 per cent in 1995-96 to 5.5 per cent in 1999-2000 and is budgeted to marginally decline to 5.1 per cent thereafter. As revenue deficit constitutes over 70 per cent of fiscal deficit, the borrowing incurred does not create productive capacity in the economy but only increases outstanding liabilities and feeds back into higher revenue expenditures through increased interest payments. Thus, capital expenditure as a proportion of GDP has declined from 4.4 per cent in 1990-91 to 2.5 per cent in 2000-01. At the same time, the outstanding internal liabilities of the central government in 2000-01 were estimated at 51.5 per cent of GDP and interest payments constituted 4.6 per cent of GDP.

05.1.2 Achieving fiscal consolidation is important from the viewpoint of ensuring both macroeconomic stability and balance of payment equilibrium. At the same time, it is important to increase capital outlay and ease pressure on interest rates not only to improve the poor state of physical infrastructure prevailing at present, but also to improve the slackening aggregate demand in the economy.

05.1.3 An important reason for increasing fiscal imbalance at the central level is the low and declining ratio of tax revenue to GDP. The tax/GDP ratio has declined by over one percentage point from 10.1 percent in 1990-91 to about 9.0 percent in 1999-2000 (see Table on page 14). Analysis shows that the revenue from direct taxes as a proportion of GDP has shown an impressive increase from 1.8 per cent in 1990-91 to 3.4 per cent in 2000-01. In contrast, revenue from excise and customs has declined sharply from 7.9 per cent to 5.5 per cent, during this period. While the declining revenues from customs duties at a time when the economy is set to liberalise its external trade is not surprising; the decline in the revenue productivity of excise duty by one percentage point is worrisome. Increasing revenue productivity of internal indirect taxes is critical to improving the revenue ratio, reducing revenue and fiscal deficits and achieving fiscal consolidation.

TABLE
TAX-GDP RATIO PERCENTAGE

Years	Income Tax	Corp.Tax	Excise	Customs	Total
1990-91	0.9	0.9	4.3	3.6	**10.1**
1995-96	1.3	1.4	3.4	3.0	**9.4**
1998-99	1.2	1.4	3.0	2.3	**8.2**
1999-2000	1.4	1.5	3.1	2.4	**8.8**
2000-01 (RE)	1.6	1.8	3.2	2.3	**9.0**
2001-02 (BE)	1.6	1.8	3.3	2.2	**9.2**

Source: Annual Economic Survey, 2000-2001

05.1.5 From this perspective, expansion of the tax base by extending the tax on services is extremely important. As service sector has grown faster than both primary and secondary sectors, extending the tax to this sector is important to realise revenue from the increasing activity in this sector. This is also necessary from the viewpoint of a fair distribution of the tax burden on different sectors of the economy. In addition, development of a scientific and well coordinated system of domestic trade taxes is possible only when the base of the tax is extended to cover the consumption of all services. For these reasons various institutions and fiscal experts have strongly recommended a comprehensive coverage of service sector under the tax net.

05.2 Economic Principles of taxing services:

05.2.1 We have, in our approach to expanding the base of service tax, kept some important principles in the background. In our view, the expansion of service tax base should be done in the context of the overall objective of simplification and rationalisation of the tax system. In this, the issues of efficiency, equity and administrative feasibility are as important as that of improving the revenue productivity. It is also important to recognise the interdependence of goods and services in the production and distribution activities in the economy in designing and implementing the tax system.

05.2.2 As already mentioned, the most important objective of the reform exercise is to broaden the tax base and eventually integrate the base of the service tax with taxes on goods. What is intended in the process is revenue generating tax reform. Increase in the base of the tax should not only result in increasing revenues in the short run but also enhance the revenue productivity of the tax system in the medium and long run. Notably, in all growing economies, service sector has been an engine of economic growth. Further, it is also observed that the consumption of services increases faster than the increase in incomes, for the richer sections of community consume disproportionately higher proportion of their incomes on services as compared to the poorer sections. Therefore, extending the tax to the services sector is desirable also from the viewpoint of both horizontal and vertical equity.

05.2.3 In making our recommendations to expand the tax base to all tradable services, we have been guided by the principle of neutrality, as well. At present, the burden of taxation is borne mainly by the consumers of goods and not services. This favourable tax treatment causes the resources to be allocated in favour of the latter. Selective taxation of services covers only about 5 per cent of the activity in the service sector leaving 95 per cent of the sector untaxed. This lopsided distribution of tax burden on goods tends to affect consumers' choice in favour of consumption of services vis-à-vis goods. It is our considered view that unless there are compelling reasons for exempting certain services, all services should be taxed to achieve neutrality in taxation. This, of course, would leave public services, services of meritorious nature, those with significant externalities and those that are in the unorganised sector and therefore, difficult to administer, outside the tax net.

05.2.4 In our view, it is important that the taxation of services should be structured in the context of the medium term objective of evolving a manufacturing VAT at the central level by merging the tax on services and goods with the CENVAT on goods. Integrating the tax on services with the CENVAT implies that it should be leviable at a uniform rate with goods and with full credit given to input tax paid on both goods and services. As the services enter into the manufacture of goods and vice versa, a full-fledged VAT will provide input tax relief on all taxed inputs irrespective of the inputs being goods or services. The transition to full-fledged VAT as mentioned above should be kept as the target to be achieved in 2004-05 and reforms should be calibrated to facilitate this transition.

05.2.5 We firmly believe that the design and implementation of the service tax should give due consideration to efficiency in resource allocation. This implies that the tax system should be simple, transparent and broad-based and should have a low rate without being cascading in nature. We are aware that all pre-retail taxes such as excise duty would have cascading elements. This however, is a limitation placed by the Constitutional arrangement and our task is to recommend the design and implementation of the tax system to minimise distortions within the framework given by the Constitution. This calls for providing full relief on the taxes paid on inputs. However, until such time as full-fledged VAT can be levied, it is necessary to ensure that the tax rates are kept at a low level so that cascading is minimised.

05.2.6 The Expert Group has also considered the aspect of administrative feasibility and convenience in formulating its recommendations. This calls for the exemption of the services provided by the unorganised sector and keeping the small service providers outside the tax net. We are aware that this could lead to bunching and splitting around the threshold value. However, that would be more acceptable than having to administer the tax on a large number of small service providers. Besides, excluding the small service providers from the scope of taxation makes administration simple, keeps administrative and compliance costs low and avoids harassment to such small service providers. Eventually, when a full-fledged VAT comes into vogue, self enforceable nature of the tax may prompt many small service providers to voluntarily register and pay the tax at the prescribed rate, for exemption from the tax will lead to cascading of input taxes and thereby may make their services non-competitive. This is particularly so in the cases of those services which are predominantly in the nature of inputs.

05.2.7 While extending the scope of the tax to cover services, it is important to ensure that this does not hinder economic growth and reduce consumption entitlements of the poorer sections of society. This implies that the tax base should have a small and selective negative list. However the selective exemption list should really be small and in choosing the same, it is essential to take into account the degree of externalities, merit good elements, distributional considerations and administrative feasibility. At the same time, the exempted list can not remain unchanged for all times to come and therefore, the government will have to review the list from time to time in accordance with the changing socio-economic societal conditions and perceptions.

05.3 The existing structure of service tax law and procedures and their inadequacies:

05.3.1 The service tax has been imposed by the Central Government in exercise of powers vested in it under residuary entry no. 97, list-I of the seventh schedule to the constitution. As indicated earlier, this tax was first imposed in 1994. At the time of imposition, certain provisions for levy of this tax were made in the corresponding Finance Bill, which was later enacted as the Finance Act, 1994. The provisions contained in Chapter V of the Finance Act, 1994 have continued to govern the levy of service tax even though the scope of this tax has considerably expanded, over the years. The procedure for levy of service tax is provided in Service Tax Rules, 1994.

05.3.2 The provisions contained in Finance Act, 1994 basically relate to defining the taxable services, service providers, value of taxable services and the taxable event. It also contains provisions for assessment, demands, penalty, revision, and appeals. A number of provisions of the Central Excise Act, 1944, i.e., those mainly relating to refunds, power to summon, adjudications, powers of the Central Board of Excise & Customs etc., have also been made applicable to service tax. The provisions for settlement of cases, advance ruling etc., which are essential features of any progressive tax law, are conspicuous by their absence. This is evidently an ad-hoc legislative arrangement.

05.3.3 The Finance Act, 1994 contains specific definitions for each of the services, service providers, and value of taxable services. These provisions appear to have been incorporated in accordance with the selective approach adopted for taxation of services. However, such specific definitions give rise to serious problems of interpretation between the department and the assessee. While the departmental authorities interpret the definitions in their widest amplitude so as to cover maximum number of service providers, the assessees normally take the narrowest meaning possible so as to exclude themselves from the tax net. Further, the selective approach to taxation gives rise to allegations of discrimination leading to increased litigation. The ill effects of such provisions are underlined by the fact that around 321 petitions are pending in various High Courts all over the country, regarding service tax.

05.3.4 It has been a generally accepted view that the legislative and procedural structure for administration of service tax is not at par with the other taxes resulting in poor realization from most of the services. The Comptroller & Auditor General of India, in a Systems Appraisal Report submitted in March 2000 has also adversely commented upon this aspect. The C&AG has pointed out that inadequate and staggered coverage of services along with the exclusion of certain sub-segments of services covered, has led to serious shortfalls in revenue realization vis-à-vis the tax potential.

05.4 Questionnaire & Responses:

05.4.1 As indicated earlier, we had prepared and circulated a questionnaire **(Annexure-I)** to seek opinion of various trade bodies, Government and regulatory agencies as well as certain renowned economists and fiscal policy experts, regarding the scope of our work. A copy of the questionnaire was also forwarded to all State Governments for their comments. The list of respondents is placed at **Annexure-II.**

05.4.2 Among the trade bodies, most of the prominent industry federations have responded to our request. Similarly, many service providers associations have also responded. Prominent among the trade bodies and associations who have responded to the questionnaire are ASSOCHAM, FICCI, PHD Chamber of Commerce & Industry, All India Motor Transport Congress, Indian Institute of Architects, Institute of Chartered Accountants of India, Institute of Cost & Work Accountants of India, Institute of Company Secretaries of India, Express Industry Council of India, Bar Council of India, Cellular Operators Association of India, Travel Agents' Federation of India, and The Bombay Custom House Agents' Association. Most of these associations agreed with the rationale behind the imposition of service tax and supported the effort to expand the tax base. They requested for a simple and transparent administrative system with a separate enactment for service tax.

05.4.3 We have been immensely benefited by the responses from eminent economists and fiscal policy experts. Dr. Raja J. Chelliah, who headed the Tax Reforms Committee in early 1990s based on whose recommendations the service tax was imposed for the first time, sent a detailed response. Dr. Chelliah recommended comprehensive coverage of all goods and services, domestically produced as well as those imported, under the tax net. He has suggested the extension of input tax credit to the service sector with corresponding increase in the tax rate to make it revenue neutral. Dr. Arindam Dasgupta suggested a common rate of ad-valorem tax for all goods and services, with very few exemptions. In his view, the unorganised sectors should be covered by presumptive taxation with established norms used by CSO in compiling national accounts instead of a threshold exemption as the latter course leads to tax avoidance and fragmentation. He also suggested exclusion of owner occupied housing sector, classical financial services, rural and public sector medical service providers, Government aided and Government run schools from the purview of service tax. Dr. Parthasarathi Shome, who interacted with us during our fourth meeting, was of the opinion that the ideal system for indirect taxation is a comprehensive and integrated VAT on goods and services in which both centre and states participate. In this background, he suggested the coverage of all services comprehensively with a well-defined negative list and exclusion of unorganised sectors by prescribing a reasonable threshold limit. In his view, conceptually there is no limitation in imposition of tax on social sector services such as education and health. Many countries in South America, New Zealand, Ireland, Turkey etc., tax the service providers in these sectors. Dr. Shome further opined that there should be no hesitation in imposing the service tax on railways, air transport and road transport, either. A few senior tax administrators viz., Shri S.V.Iyer and Dr. A.K.Bandopadhyaya also forwarded their views.

05.4.4 Among the states, only the Governments of Uttar Pradesh, Bihar, Karnataka, Punjab & Kerala responded to our questionnaire. These states underlined the need for providing more avenues for raising tax resources for State Governments and requested for assignment of powers to tax select services to the states to help in mobilizing these additional resources.

05.4.5 The Reserve Bank of India forwarded two notes on "Taxation of Financial Services" which inter-alia supported the imposition of service tax on such services but highlighted certain difficulties in administering the same. The Railway Board, in its brief reply, stated that the railway services may not be brought under the tax net as any imposition of such a tax would lead to additional burden on ultimate consumer. It may also adversely affect the rail traffic which considering the prevailing financial crisis, the railways could ill afford.

06. RECOMMENDATIONS:

06.1 Coverage and time frame:

06.1.1 As discussed earlier, the service tax is presently levied on a number of select services which have grown from 3 in 1994 to 26 in 2000. In the budgetary proposals for the forthcoming financial year, the Government has proposed the addition of 14 more services to the tax net. In our view, this selective approach to the taxation of services is undesirable for this violates neutrality in taxation, leads to inadequate coverage in addition to raising several avoidable procedural/legal complications. Systemic approach to service taxation requires general and comprehensive extension of the tax to cover all services with a small and clearly defined exemption list. The exemption list will have to be carefully vetted for administrative feasibility, merit goods and externality reasons and distributional considerations.

06.1.2 Balancing the requirement of higher revenue mobilization with public good, would be possible if the comprehensive coverage is tempered by a well defined negative list of services which are to be kept out of the tax net. The services relating to public utilities such as water supply, sewerage etc., those relating to sovereign functions of the state and those services, which are essentially meritorious, should be placed in this negative list. These services include services relating to civil administration, defence, internal security, courts of justice, jails, intelligence, revenue services, strategic research and development and international affairs.

06.1.3 The feasibility of taxing education and health services has been considered by us in detail. Provision of primary education and health facilities is one of the basic functions of any welfare state. In any case, as per the directive principles enshrined in our constitution, provision of these facilities is the duty of the state. Further, provision of basic education and health services in a country like ours with very low standards of human development, eminently qualifies as "merit goods". In this view of the matter, we have already recommended that all school education upto class twelve or equivalent should not be subject to taxation. Similarly, certain basic health care, preventive medicine and family welfare services should be exempted. Barring these exclusions, other services in these sectors should be taxed at par with the services in other sectors. We reiterate these recommendations.

06.1.4 The evolution of a destination based consumption type CENVAT on goods and services presupposes that all exports of goods and services should be exempted from the tax net. This requires that any services produced in the country but supplied outside the country should be exempted whereas the services produced abroad or supplied from outside the country for consumption in India should suffer the tax incidence on the same basis as the services produced and supplied within the country. The services supplied to the foreign nationals and institutions within India should also be taxed. Upon eventual evolution of manufacturing stage VAT, the tax on exports could be zero-rated. In the interim all the exported services should be exempted.

06.1.6 A list of services which should be kept outside the purview of service tax was drawn by us and is annexed to our interim report. The same is reproduced in **Annexure-III** to this report, for ready reference.

06.1.7 In respect of certain activities, which are covered under the service sector, the constitution specifically empowers the State Governments to levy taxes. These include taxes on entertainment, electricity, carriage of passengers and goods through road and inland waterways. Therefore, imposition of service tax on these activities separately by the Central Government, has been considered by us in light of the constitutional/legal position. In this regard, we have been benefited by the legal advise provided by Shri S.B.Jaisinghani, Additional Solicitor General of India. We have been advised that the levies mentioned in the state list, in the seventh schedule of the constitution, are the taxes, which are imposed directly on the users of these services whereas the service tax is an indirect tax on the service providers. Therefore, it would be constitutional and legal for the Central Government to impose a service tax on these activities irrespective of their being covered by any state level taxes.

06.1.8 In the interim report, we had recommended that the comprehensive coverage of service sector could be implemented from 2001-2002 onwards. Whereas, the tax on services could be integrated with CENVAT on goods to evolve into a comprehensive levy on goods and services by 2004-2005. We have considered this further, specially in light of the budget proposals for 2001-2002. In our view, it may be still possible for the Government to implement the comprehensive coverage as a mid-year measure during 2001-2002 itself.

06.2 Exemptions:

06.2.1 Another important aspect relates to exemptions. There are certain services which the Government may like to exempt for developmental reasons, for the time being. Some of these services such as classical banking services relating to deposits and loans, basic financial intermediation services, and information technology sector were identified by us and illustrated in our interim report.

06.2.2 Subsequently, we have considered the issue of exemptions further. The Directorate of Service Tax has carried out a study to identify the service sectors to be exempted, on the basis of WTO classification of service sectors. A copy of WTO classification is placed at **Annexure-IV**. Since this is an internationally accepted classification, it is felt that a consideration of exemptions, on the basis of such classification, would be more systematic.

06.2.3 It is observed that the WTO classifies the services broadly in 12 sectors. The sector-wise list of proposed exemptions is annexed at **Annexure-V**. We may state here that due to paucity of time and non-availability of explanatory material, it has not been possible to carry out an exhaustive exercise. The proposed exemptions are, therefore, illustrative in nature.

06.2.4 While the sector-wise list of exempted services has been prepared keeping in view the socio-economic and developmental parameters, it is also necessary to consider the administrative feasibility and convenience for deciding on exemptions. This raises the issue of taxing the services provided in the unorganised sector and by small service providers. The alternative approaches to address this issue have been discussed by us in our interim report. One way to exclude the unorganised sector from the purview of tax is to prescribe a threshold on turnover and exempt the service providers below the prescribed threshold limit from the payment of tax. Alternatively, the service providers having a turnover upto a prescribed limit could be taxed on presumptive/compounded basis.

06.2.5 We have considered these alternative approaches. We are aware that prescribing a threshold to exempt small service providers can lead to tax avoidance by splitting around the threshold value. On the other hand, we are also aware that the systems of presumptive taxation and compounded levy have not been particularly successful in our country. In fact, on the Central Excise side, the Government has been progressively dismantling the compounded levy regime on select commodities and has been bringing these commodities under the regular tax regime. Therefore, on the balance, we are of the opinion that it may be more appropriate to exempt unorganised sector and small service providers altogether from the tax net by prescribing the threshold exemption limits.

06.2.6 In our interim report, we have recommended that, for the time being, it would be desirable to keep the threshold at Rs.10 lakhs. This limit was determined on the basis of a study conducted by the Directorate of Service Tax on the existing taxpayer profile of 7 major Central Excise Commissionerates, which reveal that while 79.25 percent assessees were having a turnover below Rs.10 lakhs, they contributed only 2.9 percent of the total receipts during 1999-2000. The exclusion of such large number of assessees with very low revenue potential would reduce the cost of collection considerably. Additionally, stipulating a reasonable threshold also makes the tax system more efficient and acceptable. Therefore, we reiterate our earlier recommendations. We also suggest that this threshold limit of Rs.10 lakhs could continue until a transition is made to comprehensive VAT on goods and services, when the thresholds for goods and services could be standardized.

06.3 Input tax relief:

06.3.1 The imposition of a commodity tax without providing for relief on tax incidence suffered by the inputs, is inherently regressive and leads to double taxation. Therefore, the expansion of input credit mechanism is a universally accepted practice and the importance of the same bears no reiteration.

06.3.2 However, the present system of taxation of services does not provide for input tax relief. Perhaps, in the initial stages, the Government did not want to complicate the tax administration by providing for such relief. The moderate rate of tax of 5 percent may have been another factor responsible for absence of such a relief mechanism. With the proposed comprehensive coverage of service sector and its eventual merger with the CENVAT, it would be necessary to extend the system of input tax relief to service sector, as well.

06.3.3 As a first step, we would suggest that input credits may be extended within the service sector to the service inputs only. An appropriate scheme for providing tax credits in respect of service inputs used for supply of services by a service provider could be configured. The tax authorities could draw upon the experience gained from Modvat scheme on the Central Excise side while formulating the input credit scheme for service sector. The scheme for extension of credits on service inputs would enable the tax authorities to gain sufficient experience and help them in smooth implementation of comprehensive levy on goods and services.

06.3.4 While making these recommendations, we are conscious of the fact that many services are used as inputs in the manufacture of goods and vice-a-versa. Therefore, a totally revenue neutral system would require extension of inter-sectoral credits between goods and services. Considering that there is no input credit mechanism within the service sector presently, we are of the opinion that a scheme for such inter-sectoral credits can be properly implemented only after the tax authorities have gained sufficient experience in allowing intra-sector credits, i.e, within the service sector, as indicated above. The inter-sectoral credits between goods and services could be permitted upon merger of service tax with CENVAT.

06.4 Rate structure & revenue potential:

06.4.1 The service tax is presently levied at a moderate rate of 5 percent. The low rate of tax is, perhaps, justified as there is no input tax credit mechanism. In our view, the present rate of 5 percent could continue till the service tax is integrated with CENVAT. Upon such integration, the tax will have to be levied by determining a revenue neutral uniform rate.

06.4.2 The Government has broadly rationalized the Central Excise duty structure by providing for a single CENVAT rate of 16 percent with a Special Excise duty slab. In case of certain essential items, a special rate of 8 percent has also been prescribed. We presume that the single basic rate of 16 percent will be extended to cover almost all commodities by the financial year 2002-2003. Simultaneously, the Government would be well advised to work towards a uniform rate for service tax and CENVAT by April 2004. Upon eventual integration of these two taxes, a revenue neutral rate could be worked out.

06.4.3 Until such time as service tax is integrated with the CENVAT, as mentioned above, the tax rate could be kept at 5 percent. This tax rate is recommended for the present even after the extension of input tax relief within the service sector, as the moderate levy at this rate would considerably mute any resistance to expansion of tax base on comprehensive basis.

06.4.4 As indicated earlier, the service sector presently contributes more than 50 percent of the national GDP. Therefore, this sector promises immense revenue potential. Accordingly, upon comprehensive coverage of service sector, the receipts from service tax are likely to increase significantly. Though it is difficult to clearly estimate the likely revenue gain because the number of services and the volume of activity covered by this sector is enormous, the estimates made by M/s. Arthur Andersen in respect of certain key sectors namely, transportation and storage, post and telecommunications, banking and financial institutions indicate that the tax base will be extended by Rs.68,857 crores by addition of these services to the tax net. A summary of these estimates was already incorporated by us in the interim report, which is reproduced (with some modifications) in this report at **Annexure-VI**, for ready reference.

06.4.5 Imposition of service tax on transport sector has been a contentious issue. The levy of service tax on Goods Transport Operators (GTOs) in the past had led to various administrative and legal problems. We had also discussed this issue with their representative body, i.e., All India Motor Transport Congress (AIMTC). The major opposition to this tax seems to arise on two counts. Firstly, imposition of tax only on GTOs is discriminatory vis-à-vis railways and secondly, a majority of operators is in the unorganised sector. So far as, the railways is concerned, the negative views of the Railway Board regarding imposition of tax on railway services have been already summarized by us, earlier in this report.

06.4.6 We have given considerable thought to this issue. Our views have been already indicated in the interim report. We are of the opinion that railway services present a area of huge potential for taxation. The income of railways from freight and passenger travel amounted to Rs.31,575 crores in 1999-2000. We had, in our Interim Report, indicated that the Government may decide to exempt freight revenues of essential commodities and passengers travelling by ordinary class from service tax. However, upon reconsideration, we are of the opinion that such selective exemptions may not be advisable; primarily because such exemption would be discriminatory vis-à-vis transport of essential commodities and passengers by road transport operators. Therefore, a minimum receipt of Rs.1500 crores can be estimated from taxation of railway services. This huge chunk of revenue will be received from a single service provider with consequent ease of administration and minimum cost of collection. As such, in the interests of augmentation of public revenue, we are not inclined to accept the views of the Railway Board. Further, in case, the Government accepts our recommendations to impose service tax on railways, the basic objections of GTOs to imposition of such a tax on road transport sector will be taken care of. Additionally, the recommendation for threshold exemptions would exclude the small transport operators from the tax net. Therefore, we believe that the imposition of service tax on entire transport sector, without any discrimination, would make it more acceptable to the service providers.

06.4.7 The air transport sector suffers special levies, i.e., inland air travel tax, foreign travel tax etc. Similarly, the hospitality sector pays luxury tax, expenditure tax in addition to the usual commodity taxes. Since, multiple taxation on the same base is not a healthy practice, we have suggested that the Government may consider rationalizing the tax system taking a holistic view at an appropriate time. Though, the efforts at rationalization of various levies on these sectors may result in some revenue sacrifices, in the interest of simplification and reducing the tax burden on these important sectors, we reiterate this suggestion.

06.5 Separate enactment for Service Tax:

06.5.1 The service tax is presently administered through the provisions made in Chapter V of the Finance Act, 1994 and the Service Tax Rules, 1994. Additionally, a number of provisions of the Central Excise Act, 1944 have been made applicable to the service tax matters. We have already discussed the inadequacies of this legal framework. It is our considered view that smooth implementation of service tax levy on a comprehensive basis may not be possible within the parameters of existing law. Therefore, we recommend a separate self-contained enactment to administer service tax.

06.5.2 While making this recommendation, we are conscious of the fact that this separate enactment would be operational only during the transition period of eventual merger of service tax into comprehensive CENVAT on goods and services. In view of this limited period of operation, it is possible to contend that the effort of enacting a separate law may not be worthwhile. However, we feel that the comprehensive coverage of service sector with a well defined negative list requires total legal clarity for proper implementation. Further, some legislative provisions specific to service sector also need to be incorporated. All the trade bodies interviewed by us have stressed the need to have a modern legislative provision and a forward looking administration for service tax. We are also of the opinion that a separate enactment, in the transition period, would help in crystallizing the issues specific to service sector which would enable the Government to address them better while merging the service tax with Central Excise duties. In other words, it would be helpful if the law, which may be enacted for administration of comprehensive levy on goods and services, is drafted on the basis of experience gained from a separate service tax law, in addition to the age-old law governing the Central Excise duties.

06.5.3 Our views regarding definitions of certain crucial concepts and expressions under the proposed enactment, have been incorporated in the interim report. Therefore, we are not repeating the same. Suffice it to say that the taxation of services should cover all commercial transactions other than those involving goods and immovable property. The service tax being an ad-valerom levy, the concept of value is also important. We recommend that this tax should be levied on the basis of transaction value i.e., the price actually received or receivable for the services supplied, which is also the international practice in respect of all commodity taxes.

06.5.4 The service tax enactment should aim at minimising the scope of disputes and litigation by reducing the discretionary powers of the tax authorities. A provision for self-assessment with facility to file a revised return, fixed penalties for technical offences, provisions for settlement of cases and advance ruling on substantive tax related issues are some other features, which we would strongly recommend for being incorporated in the law.

06.5.5 We understand that the Directorate of Service Tax has forwarded a self contained draft law for levy and collection of service tax for the consideration of the Government. We hope that the Government would be able to consider this at an early date so that the same could be processed and enacted within a short period.

06.6 Merger of Service Tax with CENVAT:

06.6.1 In our interim report, we have recommended that the tax on services should be eventually integrated with CENVAT on goods to evolve into a comprehensive CENVAT on goods and services by 2004-2005. This would essentially require following steps.

(i) Broadening the tax base to cover all services except a few public services and services with strong merit good element;

(ii) Provide relief of tax paid on inputs and capital goods both on goods and services;

(iii) Integrating service tax with CENVAT to levy tax at a uniform rate with standardized threshold exemptions, both on goods and services.

06.6.2 We have already recommended the expansion of tax base to comprehensively cover all services with a small but well defined negative list. We have also recommended that as a first step input tax relief should be immediately provided within the service sector. It has been suggested that as we gain experience in administering the service tax with service related input credits, it would be possible to estimate the tax base of services more accurately which could in turn be used to determine a revenue neutral tax rate for integrating the service tax with CENVAT on goods.

06.6.3 We had expected that the Government would be expanding the base of service tax on comprehensive basis, as per our recommendations, from the next financial year, i.e., 2001-2002. Perhaps, it was not possible for the Government to take a final view on our interim recommendations by the time the budgetary proposals were firmed up. However, considering the intrinsic merits of our recommendations, we hope that this may come about as a mid-year measure. We presume that the excise duty structure on goods may be further rationalized to achieve a single basic rate of CENVAT, by April 2002. At the same time, the modalities for merging the tax on services with that on goods should be worked out and the detailed logistics relating to levy of VAT at a manufacturing stage should be calibrated. In April 2003, the tax rate on services and that on goods should be made uniform. The threshold for goods and services should be standardized and details of procedural and administrative mechanism to allow inter-sectoral input stage credit should be worked out. This could then lead to merger of service tax with CENVAT on goods by 2004-2005.

06.6.4 We have suggested, in our interim report, that the service tax should be administered on the basis of a fully computerized web-based tax administration system, to evolve into the first e-tax in the country. All routine formalities like registration, submission of returns and payment of tax could be complied on line thereby reducing the taxpayer-assessor interface. We recommend that similar administrative system may be implemented in respect of CENVAT operations also so that upon eventual merger, the comprehensive tax on goods and services is administered on the basis of computerized information systems.

06.7 Assessment and audit procedures:

06.7.1 In our interim report, we have suggested that the existing assessment and audit procedures for service tax should be completely overhauled to implement a self assessment based system of tax administration. We are pleased to note that the Government has accepted our recommendations and proposed certain legal amendments in the Finance Bill, 2001.

06.7.2 A self assessment based tax administration presumes appropriate audit/risk based scrutiny of returns and enforcement. We had requested M/s. Arthur Andersen to ascertain the international practices in this regard. Their report indicates that the taxation system in most of the developed countries envisage a twin approach to audit. The selective audit by departmental authorities of the records and returns of the service providers is based on normative parameters to be evolved on risk basis. These parameters should be determined by experts on the basis of experience gained in implementation of service tax, till now.

06.7.3 We would also suggest that the assessees liable to pay service tax on gross receipts, which exceed a predetermined limit, should be required to get their accounts audited by professional chartered accountants/auditors, as well. The accountants/auditors should specifically comment regarding accounting systems of the assessee companies and certify full tax compliance of these systems. We feel that such statutory audit would not place any additional burden on the assessees as they are already required to get their accounts audited in terms of the provisions of other laws, such as the Companies Act and the Income Tax Act. However, to avoid duplication, the threshold beyond which such audit certification is necessary, could be standardized with other tax laws.

06.7.4 In case of recalcitrant assessees or the cases where systematic tax evasion is suspected, tax authorities should be empowered to order special audit at the cost of Department, if need be by involving professional auditors of repute. The provisions to this effect could be in line with similar provisions for cost audit under the Central Excise law.

06.8 Administrative arrangements:

06.8.1 A well-defined administrative system and structure are pre-requisites for successful implementation of any tax measure. The service tax is presently administered by Central Excise Commissionerates working under the Central Board of Excise & Customs (Board). Since, the tax base and revenue generated has been comparatively low, a clear-cut system and earmarked structure for service tax are yet to take shape.

06.8.2 The comprehensive coverage of service sector with wider tax base and internal credit mechanism would require dedicated policy formulation and efficient administration. It is suggested that a separate division should be created in the Board to exclusively deal with service tax matters. This would enable proper attention being paid at the stage of policy formulation and coordination.

06.8.3 The Directorate of Service Tax could be developed into a hub for tariff research, technical coordination and administrative direction. For this purpose, a regular establishment with adequate staff and budgetary grants needs to be put in place. In order to attract willing officers with right talent and aptitude, the Board could also consider payment of deputation allowance in line with the practice in respect of other Directorates under its administrative control. The administrative relationship of the Directorate with the field formations should also be clearly defined.

06.8.4 The staff deployed for service tax work is drawn from Central Excise formations. In most of the cases, the officers carry out Central Excise and Service Tax work simultaneously. It would be appropriate if the department earmarks the staff required for service tax work separately so that this work receives their undivided attention.

06.8.5 We observe that the service tax receipts in the metro/mini-metro Commissionerates are substantial and we accordingly recommend creation of separate Service Tax Commissionerates at Mumbai, New Delhi, Chennai, Calcutta, Bangalore & Ahmedabad. We also suggest that separate service tax Divisions may be created in other cities/moffussil Commissionerates for exclusively dealing with the service tax work. As usual and to begin with, the Chief Commissioners in charge should also supervise the functioning of Service Tax formations until growth in service tax revenue or complexities of work warrant a review.

06.8.6 The present system of registration, levy, assessment and collection of service tax is totally manual. The Directorate of Service Tax has proposed a computerized online web-based tax administration system so that service tax could be administered as the first e-tax in the country. M/s. CMC Ltd has already conducted a system feasibility study. Implementation of such a system would require certain capital expenditure initially but would prove cost effective in the long run. We would recommend that the Government should immediately bestow its attention on this aspect and provide adequate resources to the Directorate of Service Tax and field formations for this purpose.

06.8.7 Inter-linked with the specific needs of staff and grants is the broader issue of financial autonomy for tax collecting agencies in the country. We are informed that the Government is already examining this issue. Therefore, we would only mention here that vesting the tax authorities with greater flexibility in regard to resource management is imperative for enforcing accountability.

06.9 Publicity and taxpayer education:

06.9.1 We have recommended for comprehensive coverage of service sector under service tax with a well-defined negative list. However, the concept of comprehensive coverage has been tempered with the exclusion of small service providers and those in the unorganised sector by way of a threshold exemption limit of Rs.10 lakhs. In their entirety, our recommendations seek to give shape to a fresh and potent limb of indirect taxation at par with Central Excise duties.

06.9.2 This is a major step in broadening the tax base. Therefore, it is necessary that it should be widely discussed in public fora so that the issues involved are properly appreciated and well understood. We are also aware that the incidence of service tax falls upon comparatively well off sections of the society. Therefore, the resistance to this measure is also likely to arise at a more vocal and focused plane. As such, it is necessary that the implementation of our recommendations is accompanied by a well aimed publicity campaign through print and audio-visual media.

06.9.3 The publicity campaign should be aimed at educating, preparing and persuading the taxpayers for improved voluntary tax compliance by explaining the scope and special features of the service tax. The taxpayers should also be prepared for a gradual move towards a full-fledged goods and services VAT.

06.9.4 Keeping in view the objectives set-out hereinbefore, this campaign should be ideally carried out in two phases. The phase-I could highlight the rationale for expanding the tax base and raising more resources, especially in view of the stagnating growth of other indirect taxes as well as declining tax to GDP ratio in the country. It should further highlight the fact that this is a moderate levy with simple and transparent administrative systems and procedures, which are in line with the international practices. The phase-II is suggested to be an ongoing campaign focused inter-alia on taxpayer education/assistance through audio-visual publicity. All forms, returns, manuals, brochures, circulars etc. should be drafted and prepared well in advance in a simple format so as to reach the target group without any hitch and should be capable of electronic dissemination/submission.

06.9.5 Considering the limitations of Government run publicity agencies like DAVP and the Directorate of Publications etc., it is suggested that the phase-I of this campaign may be assigned to a professional public relations/advertising agency. Adequate budgetary provisions should be made in a need based manner for a sustained campaign.

06.10 Centre-State issues in Service Tax:

06.10.1 There has been considerable discussion regarding sharing of the power to levy tax on services with the States. As indicated earlier, various State Governments have made this suggestion in response to our questionnaire too. In the conference of Chief Ministers/Finance Ministers of the States and the Union Territories on domestic trade reforms and value added tax, held in June 2000, the

Governments of Orissa, Madhya Pradesh, Karnataka, Maharashtra & Bihar had specifically raised this issue. In this conference, the Hon'ble Finance Minister had decided that the Standing Committee of State Finance Ministers would interact with the Expert Group on Service Tax, in this regard.

06.10.2 We have repeatedly requested the Empowered Committee of State Finance Ministers to send their views on issues relating to service tax so that a holistic view could be taken. However, we are yet to receive a response from them.

06.10.3 Nevertheless in view of the importance of this issue in the context of long term fiscal policy and developing a co-ordinated system of domestic trade taxes in the country, we have appropriately considered the matter. It is our considered view that the present system of taxing services separately from goods can be a source of distortion, which should be mitigated. It has been suggested that ideally the tax on services should be integrated with those on goods all the way upto the retail stage, to evolve a destination based, consumption type retail stage VAT. It is also accepted that within the present constitutional arrangement, the ideal way to evolve a rational tax system in the medium term is to implement a dual VAT, i.e, at central level upto manufacturing stage and at state level upto retail stage.

06.10.4 In this report, we have already suggested a road-map for eventual integration of taxes on goods and services into a comprehensive VAT at central level, i.e., CENVAT. However, while making this recommendation, we are aware of the constitutional position that while the Central Government is empowered to levy tax on goods only upto manufacturing stage, it could levy tax on services right upto the retail stage. The proposed State level VAT on goods would, therefore, cover the transactions after the first sale and upto the retail stage. Thus, in our view, for evolution of comprehensive destination based consumption type VAT at the state level, sharing of powers to levy tax on services with the states is necessary. In the absence of such sharing, the state VAT will only be partial as it would not be possible to extend credit to input tax on services.

06.10.5 Two alternative models are suggested by various experts for such sharing of tax powers with the states. According to one model, the taxation powers in respect of select services may be devolved to the states on the basis of regional spread of such services. The alternative model recommends concurrent powers of taxation of services by both union and states on the basis of a standardized negative list.

06.10.6 Considering that the basic objective for recommending the sharing of taxation powers on services, is to reduce distortions in implementation of VAT, it would appear to us that devolution of tax powers on a selective basis to the states may not be appropriate. Selective sharing of tax powers would not enable the states to provide input credits in respect of tax paid on such services, which are not within their purview. This will not only increase complications in the tax system but would also lead to additional distortions.

06.10.7 The alternate model of states being given concurrent tax powers in respect of services, raises certain other complicated issues. Firstly, the constitution may have to be amended to enable both centre and states to levy tax on services concurrently. Secondly, safe guards and modalities to ensure harmonization of domestic trade taxes in the country would have to be specifically worked out.

06.10.8 While these issues would require detailed deliberations, it would appear that the Central Government should stipulate certain preconditions before the arrangements for sharing are worked out. According to us, the main preconditions could be:

(i) States should have implemented VAT in respect of goods inter-alia providing for tax credit on inputs and capital goods not only for sales and purchases within the respective state but also from outside such state.

(ii) The number of rates and rate differences between states should vary within a prescribed band. This will ensure a measure of uniformity and harmonisation in the consumption tax system in the country. The band may be worked out on the basis of consensus in the State Finance Ministers' committee in the same manner as the floor rates on commodities prescribed by them.

(iii) The specific taxes presently levied in respect of entertainment, electricity, carriage of passengers and goods by road transport and luxury taxes on hotels and restaurants should be merged with general valued added tax. This would reduce the multiplicity of taxes.

(iv) The states should follow a set of codes of conduct to prevent individual states from indulging in "race to the bottom" such as providing fiscal incentives, and indulging in tax competition.

6.10.9 In our view, the sharing of powers to tax services on concurrent basis, with safeguards as indicated above, will provide additional incentive to the states to transform the existing sales tax system into a destination based consumption type VAT at the retail level. At the same time, it would also ensure and enable orderly development of a rational and harmonized commodity tax system in the country.

07. ACKNOWLEDGEMENTS:

07.1 We would like to place on record our deep appreciation for the Directorate of Service Tax and a number of officials of the Central Board of Excise and Customs for their assistance in undertaking the researches and providing the information necessary for carrying out our task. The Directorate of Service Tax provided its valuable technical assistance and logistic support to complete this task within this short period. In particular, the contribution of Mr. Sandeep Prakash, Deputy Director, has been immense. He has taken the onerous task of managing research for us, seeking legal opinion on many a relevant issue and preparing detailed notes for the Committee meetings, besides working out the logistics. It must be noted that the Expert group has functioned without a proper office of its own and yet, has been able to function mainly due to the officials of Directorate of Service Tax and the office of Member (Budget), Central Board of Excise and Customs.

07.2 We would like to place on record our gratitude to all those respondents who have furnished answers to our questionnaire-in particular to those respondents who appeared before us for interaction from the FICCI, ASSOCHAM, PHD Chambers of Commerce & Industry, All India Motor Transport Congress Association, Institute of Chartered Accountants (Western India Regional Council), and Bombay Custom House Agents' Association, for their valuable assistance in discharge of our duties. Special mention has to be made in respect of Dr. Raja J. Chelliah, Dr. Parthasarathi Shome, and Dr. Arindam Das Gupta, fiscal policy experts who have helped us in appreciating various critical issues involved.

07.3 A special word of appreciation has to be offered to M/s. Arthur Andersen, Business Consulting Group, particularly Mr. Rajiv Dimri and Ms. Saloni Roy for the timely assistance in ascertaining Service Tax law and procedures in various other countries. They have also assisted us in ascertaining potential Service Tax base in India and in identifying key services in the Indian economy for inclusion in the tax net. Their assistance has been prompt and well documented.

07.4 Our acknowledgements are also due to Dr. S. Narayan, Revenue Secretary, Mr. P.G.Mankad, former Finance Secretary, Mr. B.P.Verma, Chairman, CBEC and Dr. Rakesh Mohan, Advisor to the Finance Minister and Chief Economic Adviser for their guidance.

07.5 Our special appreciation is due for the services of Member-Secretary, Mr. Sukumar Shankar, who had to undertake a great deal of responsibility despite his several other preoccupations for the department.

07.6 Our gratitude to several others in the Government and outside who have helped us either directly or indirectly in any manner in completion of our work.

(Dr. M. Govinda Rao)
Chairman

(Dr. Arvind Virmani)
Member

(D.B.Lal)
Member

(B. C. Rastogi)
Member

(Dr. M. G. Venugopalan)
Member

(Ashok Wadhwa)
Member

(Sukumar Shankar)
Member-Secretary

ANNEXURE-I

EXPERT GROUP ON SERVICE TAX
GOVERNMENT OF INDIA
MINISTRY OF FINANCE
DEPARTMENT OF REVENUE
CENTRAL BOARD OF EXCISE & CUSTOMS
NORTH BLOCK, NEW DELHI.

Questionnaire

I. Introduction:

The Service Tax was imposed on selected services through the Finance Act, 1994. From the initial set of three services, the scope of Service Tax has been expanded to cover 30 services, 4 of which were exempted later. In the Financial Year 1999-2000, the revenue from the Service Tax covering 26 services, was Rs.2072 Crores.

2. Services constitute a very heterogeneous spectrum of economic activities. Over the years, their contribution to the national economy has increased substantially. In the year 1998-99, the service sector contributed 46% to the national G.D.P. Currently, the contribution of service sector to the G.D.P. is estimated to be about Rs.900, 000 Crores. Further it is also estimated that at the current rate of taxation, only 5% of the service sector is being taxed. This underscores the huge revenue potential, which has remained untapped. The Comptroller & Auditor General of India in their Systems Appraisal Report on Service Tax have adversely commented upon the Govt.'s inability to tap the full potential of taxation from the service sector.

3. Taxing the service sector is important from the viewpoint of neutrality in taxation as well. While the goods are subject to both excise duty and sales tax, services are not. This tends to affect consumer choice in favour of services. Besides, as services enter into the production of goods and vice versa, this opens up vast vista for evasion and avoidance of the taxation of goods as well. As most services are consumed relatively more by higher income groups of population, the objective of equity is better served by taxing services.

4. It is well known that the Government is facing increasing fiscal and revenue deficits. India's debt burden is mounting even though the debt service ratio has declined over the years. The revenue deficit of the Centre and the States was estimated to be 6.76% of the GDP during 1999-2000 whereas the fiscal deficit was as high as 9.83% during the said period. This order of fiscal imbalance has caused

unsustainable growth of indebtedness, and has spilled over into macroeconomic imbalance and balance of payment disequillibrium. Besides, this has led to an adverse effect on capital expenditure of the Government thereby severely depleting the funds available for spending on infrastructure.

5. An important reason for increasing fiscal imbalance in the country is low and declining ratio of tax revenue to GDP. The tax/GDP ratio, which was 16.4% in 1990-91, has declined to 15% in 1999-2000. This level of taxes compares unfavourably with the levels in developed countries, which is in the range of 25% to 50%. C & AG has recommended that in order to wipe out the revenue deficit altogether, the Government must pay attention to the functioning of revenue collection and widening of tax base. In order to restore fiscal balance, it is necessary to significantly increase the tax ratio alongwith measures to contain unproductive expenditures. Raising revenues from services taxation is relatively unexplored area and there is a good deal of scope for raising revenues by widening the tax base, reviewing exemptions/incentives and ensuring strict tax compliance.

6. Various institutions and fiscal experts including the Eleventh Finance Commission have strongly recommended a comprehensive coverage of service sector under the tax net to achieve a higher buoyancy in tax to GDP ratio. In addition to broadening the base of the tax, this has been advocated also to eventually switch over to value added tax system.

7. The Government has now set up an Expert Group to review the levy of Service Tax and to make recommendations regarding the extending of tax base, rate of taxation, modalities for administration and the time frame for implementation thereof. In its first meeting held on 24.07.2000, the Expert Group decided that it would be appropriate to have wider consultation with the Trade/Associations of Service Providers as well as some eminent economists and taxation experts.

8. In light of the above facts, the Expert Group has prepared this questionnaire. The questionnaire has been structured so as to elicit your responses regarding various aspects of the levy of Service Tax including its structure, extension of tax base, administration and procedures as well as time frame for implementation of a full-fledged Service Tax Act.

<u>II. Structure of Service Tax in India and its Improvement:</u>

Q.1 Can higher buoyancy in tax revenue be achieved by any means other than enlargement of the scope of levy of service tax? What alternative sources of raising revenue are recommended to ensure higher buoyancy in tax revenue?

Q.2 Would you advocate taxation of services from the viewpoint of neutrality in taxation between goods and services?

Q.3 Which are the major services would you recommend for exemption and why?

Q.4 Would you recommend a system of compounded/presumptive payment of tax for taxing less organized services? If so, what should be the thresh-hold limit for such presumptive taxation?

Q.5 What criteria should be adopted for granting exemption to certain basic service providers engaged in public health, education, transport, community/social services and agriculture?

Q.6 Should the tax rates of different services be uniform or different? Please give reasons for uniformity or differentiation.

Q.7 Would you recommend that eventually, taxation of services should be combined with Union excise duties to evolve a Value Added Tax at manufacturing stage with inter-sectoral credit set offs? Or, would you prefer continuing with selective taxation of services?

Q.8 If service taxation should be combined with the manufacturing stage VAT, how should small/unorganized service providers be treated?

Q.9 If selective taxation of services should continued, would you recommend internal credit set offs with/without levying the tax at higher rate?

Q.10 At present, the power to levy taxes on services (excluding specified services like entertainment and amusements etc.), is vested exclusively with the Central Government. Do you think that it is desirable to devolve the power to levy taxes on services to the States to enable them to levy a full-fledged goods and service tax?

Q.11 If the States are to be given the right to levy tax on services, how can this be coordinated with the Central levy to evolve a harmonized system of commodity taxation in the country?

Q.12 Some difficulties have been expressed in regard to taxation of housing and financial and social services. What approach would you recommend to levy taxes on such services?

Q.13 What is your view in regard to taxation of computer related services such as software, internet and e-commerce? Would you recommend that these should be subject to taxation like all other services or would you recommend a gradualist approach in extending the tax to them?

III. Extension of Service Tax base and time frame for its implementation

Q.1. Do you agree with the view that widening the taxation base of services (constituting over 46% of GDP) is a viable policy option before the Central Government in the face of stagnation in the share of manufacturing/industry sector in G.D.P. and consequent falling share of revenue receipts from Customs & C. Ex. sources?

Q.2 Is the existing Service Tax base covering 5% of the Service Sector sufficient in a developing country like India? Which are the services to be included on priority in the tax net in order to yield more revenue?

Q.3 What time frame would you recommend for bringing more services into the tax net? Indicate the time frame which you would recommend to extend the tax base from existing 5% to 25%, 50% and 75%.

Q.4 It is widely known that we are unable to achieve 100% tax compliance due to the following factors:

i) Lack of awareness on part of the assessees about legal provisions and procedures;
ii) Reluctance to pay tax due to complications in the procedures and paper work involved;

iii) Graft / collusion;

iv) Reluctance on the part of the service users to bear the burden of the levy.

What specific steps would you suggest to meet these problems so as to increase the level of voluntary tax compliance?

Q.5 It is well known that any taxation measure should have a harmonious blend of carrot and stick provisions for ensuring higher tax compliance. What specific measures would you advocate in this regard?

Q.6 Under the present law, service tax evaders are penalized and interest liability is realized for delayed payment. Would you recommend prosecution of recalcitrant/habitual evaders of tax in court of law in addition to imposition of penalty and interest liability?

IV. Administration

Q.1 What are the main drawbacks, which you perceive in the administration/compliance of the existing law, on the levy of 5% Service Tax on selected 26 services?

Q.2 Service Tax is a relatively new levy in India. Would you recommend its administration by a new agency with a new identity, work culture, systems and procedures, or should it remain entrusted to the existing tax collecting agency viz. Central Excise?

Q.3 Computerization is the need of the hour. What specific electronic solution package would you recommend for the smooth functioning of the Service Tax administration in the interest of Government as well as trade and industry?

Q.4 Does the existing service tax administration in India enjoy good reputation, especially among the assessees, many of whom are self-employed professionals from the unorganized sector? If not, what improvements would you suggest to enhance simplicity, clarity and transparency in administration.

Q.5 What grievance redressal mechanism would you advocate in the administration of service tax law?

V. Procedures

Q.1 What are your specific suggestions on simplification of procedures relating to (i) Registration of assessees, (ii) Payment of taxes, (iii) Submission of returns, (iv) Final assessment, (v) Grant of refund/recovery of tax arrears?

Q.2 Any taxation statute should have at least two stages of appeal and revisional remedies. What procedural improvements would you suggest to ensure that the dispute settlement mechanism operates quickly with very little hassles?

Q.3 Would you recommend extension of the jurisdiction of the Customs & Central Excise Settlement Commission in redressal of disputes to Service Tax matters?

Q.4 Would you recommend setting up of Advance Ruling Authority for service tax matters?

Q.5 Would you recommend extension of any incentives/benefits to the highest service taxpayers, with clean track record? If so, please spell out specific details?

Q.6 Presently, the service tax assessees are required to file half yearly returns. Is this procedure satisfactory or you would like the periodicity of returns to be changed? If this periodicity is to be changed, what would be your recommendations?

Q.7 At present service tax is paid in specified branches of a nationalized banks designated as the focal point bank in each Commissionerate. There are representations for increasing the number of banks authorized to receive Service Tax payment. Would you recommend extension of the facility of payment of service tax in any of the computerized branches of nationalized banks in India as in the case of Direct Taxes?

Q.8 Would you recommend extension of electronic banking facility for service tax payees including the facility of payment of service tax liability by credit cards?

VI. General

Q.1 Would you advocate any changes in our Constitution to empower Central/State Governments to levy a comprehensive tax on goods and services?

Q.2 Do you envisage that the administration should continuously make use of the services of professional agencies to launch public awareness campaigns through audio-visual media to continuously educate both the existing and prospective taxpayers in India?

ANNEXURE – II
PART – I

LIST OF RESPONDENT (TRADE / PROFESSIONAL / REGULATORY BODIES)

1. Medical Council of India
AIWAN-E, Ghalib Marg,
New Delhi 110 002
Tel – 323 5178 / 6081

2. Dental Council of India
Kotla Road, Temple Lane,
New Delhi – 110 002
Tel – 323 8542

3. Bar Council of India
21, Raj avenue
Institutional Area, Near Bal Bhavan
New Delhi – 110 02
Tel – 323 1647/ 3231767

4. Institute of Chartered Accountant of India
Annexure, 5th Floor, ICAI's Building
Indraprastha Marg
New Delhi – 110 002
Tel – 331 2055 / 3312137

5. Institute of Cost and Works Accountants of India
12, Sunder Street
Calcutta – 700 016
Tel – (033)244 1034 / 1035

6. Institute of Company Secretaries of India
ICSI House, Institutional Area,
Lodi Road, New Delhi – 110 003
Tel – 461 7321/ 24

7. Institute of Chartered Financial Analysis of India
52, Nagarjuna Hills
Hyderabad – 500 082
Tel – 335 1071 / 3411

8. Institution of Engineers
   8, Gokhale Road,
   Calcutta – 700 020
   Tel – (033) 223 8230/ 8316

9. Indian Institute of Architects
   Prospect Chambers Annexure
   Dr. D.N. Road, fort
   Mumbai – 400 001
   Tel – (022) 204 6972
   Fax – 283 2516

10. All India Management Association
    Management House
    14, Institutional Area, Lodi Road,
    New Delhi – 110 003
    Tel – 461 7354 /355

11. National Institute of Fashion Technology
    Hauz Khas, Near Gulmohar Park
    New Delhi – 110 016
    Tel – 696 5059

12. Federation of Indian Export Organisations
    PHD House, III rd Floor,
    Opp. Aisan Games Village Complex
    New Delhi – 110 016
    Tel – 385 1310 /1312/ 1314

13. Associated Chambers of Commerce (ASSOCHAM)
    11, Community Centre, Zamrudpur
    New Delhi – 110 046
    Tel – 629 2310 / 13

14. Federation of Indian chamber of Commerce and Industry (FICCI)
    Federation House, Tansen Marg
    New Delhi – 110 001
    Tel – 373 8760/ 70, Fax – 332 9369

15. Confederation of Indian Industry (CII)
    105, Kakad Chambers
    132, Dr. Annie Besant Road, Worli
    Mumbai – 400 018
    Tel – (022) 493 1790, Fax – 493 9463

16. PHD Chamber of Commerce and Industry (PHDCCI)
PHD House
Opp. Asian Games Village Complex
New Delhi 110 016

17. Chairman
Securities and Exchange Board of India (SEBI)
Mittal Court, "B" wing, Ist Floor 224
Nariman Point
Mumbai – 400 021
Tel – (022) 285 0451-56

18. Life Insurance Corporation of India
LIC of India (Central Office)
Yogakshema Building
Jeewan Bima Marg
Mumbai – 400 021
Tel – (022) 202 1383.
Fax – 281 1049

19. General Insurance Corporation of India
Suraksha Building
170, J Tata Road,
Mumbai – 400 020.
Tel – (022) 283 3046, Fax – 283 2656.

20. Reserve Bank Of India (RBI)
Head Office (Main),
Marshall Building Annexe, Third Floor
Shoorji Vallabhadas Marg, Ballard Estate,
Mumbai – 400 001.
Tel – (022) 261 8361, 261 3995

21. Consulting Engineers Association of India
East Court, Zone 4, Core 4B
2nd floor, India Habitate Centre, Lodi Road,
New Delhi – 110 003
Tel- 460 1068

22. Advertising Standards Council of India
205, Bombay Market
M. Malviya Road, Tardeo
Mumbai – 200 034
Tel – (022) 492 9371 / 494 9440

23. National Association of Software and Service Companies (NASSCOM)
International Youth Centre
Pt. Uma Shankar Dixit Marg,
Chanakyapuri
New Delhi – 110 021
Tel – 301 5416 – 19

24. Secretary
Department of Telecom (DOT)
Sanchar Bhawan, Ashok Marg,
New Delhi – 110 001

25. Association of Basic Telecom Operators of India (ABTO)
601-B, Gauri Sadan
Hailey Road,
New Delhi – 110 001.

26. Cellular Operators Association of India (COAI)
F- 301, Gaurisadan, 5, Hailey Road,
New Delhi – 110 001.
Tel – 335 0369

27. Mahanagar Telephone Nigam Limited (MTNL)
Jeewan Bharati Tower – I
124, Cannaught Circus
New Delhi – 110 001.

28. National Stock Exchange (NSE)
124, Western Wing
Thapar House, Janpath
New Delhi – 110 001
Tel – 334 4313/ 314

29. Bombay Stock Exchange (BSE)
Ist Floor, Rotunda Building,
Dalal Street, Fort
Mumbai – 400 001
Tel – (022) 270 2066/ 265 5630

30. Federation of Hotels and Restaurant of India (FHRI)
M-75, Market Greater Kailash – Part – II
New Delhi – 110 008
Tel – 648 2690

31 Secretary
Ministry of Civil Aviation
Rajiv Gnadhi Bhawan
Safdurjung Airport Complex
New Delhi – 110 003
Tel – 461 0378

32. Association of Security Organisations of India (ASOI)
S-2, Paradise Plaza
Alaknanda Shopping Complex
New Delhi – 110 0019
Tel – 621 8445

33. Indian Association of Tour Operators (IATO)
404, Padma Tower – II
22, Rajendra Place
New Delhi – 110 008

34. All India Motor Transport Congress (AIMTC)
1/16-A
Asaf Ali Road,
New Delhi – 110 002.

35. Director General of Health Services (DGHS)
Nirman Bhawan
Maulana Azad Road,
New Delhi – 110 011

36. Bombay Customs House Agents Association
73, "C" Wing
7th Floor, Mittal Towers
Nariman Point
Mumbai – 400 021
Tel – (022) 282 4618
Fax – 285 2561

37. Travel Agents Federation of India
C/o Travel Services International
301-302 Kailash Building
Kasturaba Gandhi Marg
New Delhi – 110 001
Tel – 335 9074 – 79
Fax – 335 9103

38. Express Industry Council of India
C-609, Floral Deck Plaza,
Opp. SEEPZ Central MIDC Road
Andheri (E), Mumbai – 400 099
Tel – 834 3616, Fax – 834 3617

39. Indian Venture Capital Association
C/o Gujarat Venture Finance Ltd.
Ist Flr., Premchand House Annexe
Behind Popular House
Ashram Road,
Ahmedabad – 380 009
Tel – (079) 658 1285/ 658 0704
Fax – (079) 658 5226

40. Association of Mutual Funds of India
408, a wing, Dalamal Towers
Free Press Journal Marg,
Nariman Point
Mumbai – 400 021.
Tal – 282 5869/ 288 4554/ 232 4524/ 25
Fax – 283 1163

41. Private TV channels Association
Indian Broadcasting Federation
F-15, Chand society (Behind Arogya Nidhi Hospital)
Juhu, Mumbai – 400 049
Tel – 625 1618/ 621 0124

42. Chairman
Railway Board
Rail Bhawan
New Delhi

PART - II

LIST OF RESPONDENTS (PUBLIC FINANCE EXPERTS)

1. Dr. Raja J Chelliah
   Chairman,
   Madras School of Economics ,
   Behind Govt. Data Centre,
   Gandhi Mandapam Road, Chennai 6000020.

2. Prof U shankar
   Madras School of Economics
   Behind : Govt. Data Centre
   Gandhi Mandapam road, Chennai 600020.

3. Prof Ashok Lahiri
   Director
   National Institute of Public Finance and Policy
   18/2, Satsang Vihar Marg,
   Special Institutional Area
   New Delhi 110067

4. Dr Isher Judge Ahluwalia
   Director, Indian council for Research in International
   Economic Relations
   4th floor, Core 6A, India Habitate Centre,
   Lodi road, New Delhi 110003

5. Dr Rakesh Mohan
   Director
   National Council for Applied Economic Research
   Parisila Bhavan II
   Indraprastha Estate
   New Delhi 1110001.

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9. Dr Parthasarathy Shome
National Institute of Public Finance and Policy
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Special Institutional Area
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10. Prof C H Hanumantha Rao
Centre for Economic and Social Studies
Nizamia Observatory Campus
Hyderabad 500016

11. Prof I S Gulati
Chairman
State Planing Board
Pattom, Trivandrum 695004

12. Prof Raghavendra Jha
Indira Gandhi Institute of Development Research
Gen. Arun Kumar Vaidya Marg
Goregaon East
Mumbai 400 065

13. Dr Sikha Jha
Indira Gandhi Institute of Development Research
Gen. Arun Kumar Vaidya Marg
Goregaon East
Mumbai 400 065

14. Prof P R Brahmananda
No: 12 Kalappa Block
Basavanagudi
Bangalore 560004

15. Prof G Thimmaiah
    No: 22, BHCS layout
    Bannerghatta Road
    Bangalore 560076

16. Prof D M Nanjundappa
    Sharda Krupa
    2969, 12th Main, 4th Cross
    HAL II State, Indiranagar
    Bangalore 560038

17. Shri T R Satish Chandran
    "Jagruti" 231, 18th Cross
    Sadashivanagar
    Bangalore 560080

18. Prof Praveen Visaria
    Director
    Institute of Economic Growth
    University Enclave
    Delhi 110007

19. Prof B B Bhattacharya
    Institute of Economic Growth
    University Enclave
    Delhi 110007

20. Prof Arindam Dasgupta
    Gokhale Institute of Politics and Economics
    Deccan Gymkhana
    Pune 411004

21. Dr A Vasudevan
    Executive Director
    Reserve Bank of India
    Central Offices
    Shahid Bhagat Singh Marg
    Mumbai 400001

22. Dr S L Shetty
    EPW Research Foundation
    C-212, Akurli Industrial Estate
    Kandivali East
    Mumbai 400101

23. Dr N J Kurien
Adviser, Planning Commission
Yojana Bhavan, Parliament Street
New Delhi 110001

24. Dr Omkar Goswami
Confederation of Indian Industry
23, Lodi Institutional Area
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25. Sri A Vaidyanathan
Director
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79, II Main Road, Adyur
Gandhinagar
Chennai 600 020

26. Dr Kirti S Parekh
Director
Indira Gandhi Institute of Development Research
Gen. Arun Kumar Vaidya Marg
Goregoan East
Mumbai 400 065

27. Dr Pulapre Balakrishnan
Indian Institute of Management
RECPO Post
Calicut 673601

ANNEXURE-III

List of Services not to be covered by Service Tax

1. All public services of Government (Central, States and municipal/panchayatiraj) including Civil administration, defence, para-military, police, intelligence and Govt. Departments but excluding Railways, Post & Telegraph other commercial Departments, Public Sector enterprises, Banks & Insurance.

2. All public utility services of essential nature like water supply, sewerage etc.

3. All essential medical and family welfare services (to be defined in consultation with the Health Ministry).

4. All school education upto class twelve or equivalent.

5. Any service transactions between an employer and employee either as a service provider, recipient or vice versa.

6. Services which are exported outside India.

ANNEXURE-IV

WTO classification of service sectors

SECTORS AND SUB-SECTORS	CORRESPONDING Section B
1. BUSINESS SERVICES	
A. Professional services	
a. Legal services	861
b. Accounting, auditing and bookkeeping services	862
c. Taxation services	863
d. Architectural services	8671
e. Engineering services	8672
f. Integrated engineering services	8673
g. Urban planning and landscape architectural services	8674
h. Medical and dental services	9312
i. Veterinary services	932
j. Services provided by midwives, nurses, physiotherapists and paramedical personnel	93191
k. Other	
B. Computer and related services	
a. Consultancy services related to the installation of computer hardware	841
b. Software implementation services	842
c. Data processing services	843
d. Database services	844
e. Other	845+849
C. Research and development services	
a. R & D services on natural sciences	851
b. R & D services on social sciences and humanities	852
c. Interdisciplinary R & D services	853
D. Real estate services	
a. Involving own or leased property	821
b. On a fee or contract basis	822
E. Rental/leasing services without operators	
a. Relating to ships	83103
b. Relating to aircraft	83104
c. Relating to other transport equipment	83101+83102+

ORS AND SUB-SECTORS	CORRESPONDING CPC Section B
F. Other business services	
a. Advertising services	871
b. Market research and public opinion polling services	864
c. Management consulting service	865
d. Services related to management consulting	866
e. Technical testing and analysis services	8676
f. Services incidental to agriculture, hunting and forestry	881
g. Services incidental to fishing	882
h. Services incidental to mining	883+5115
i. Services incidental to manufacturing	884+885 (except for 88442)
j. Services incidental to energy distribution	887
k. Placement and supply services of personnel	872
l. Investigation and security	873
m. Related scientific and technical consulting services	8675
n. Maintenance and repair of equipment (not including maritime vessels, aircraft or other transport equipment)	633+ 8861-8866
o. Building-cleaning services	874
p. Photographic services	875
q. Packaging services	876
r. Printing, publishing	88442
s. Convention services	87909*
t. Other	8790
COMMUNICATION SERVICES	
A. Postal services	7511
B. Courier services	7512
C. Telecommunication services	
a. Voice telephone services	7521
b. Packet-switched data transmission services	7523**
c. Circuit-switched data transmission services	7523**
d. Telex services	7523**
e. Telegraph services	7522
f. Facsimile services	7521**+7529**
g. Private leased circuit services	7522**+7523**
h. Electronic mail	7523**
i. Voice mail	7523**
j. On-line information and database retrieval	7523**
k. Electronic data interchange (EDI)	7523**
l. Enhanced/value-added facsimile services including store and forward, store and retrieve	7523**
m. Code and protocol conversion	n.a.
n. On-line information and/or data processing (including transaction processing)	843**
o. Other	
D. Audiovisual services	
a. Motion picture and video tape production and distribution services	9611
b. Motion picture projection service	9612
c. Radio and television services	9613
d. Radio and television transmission services	7524
e. Sound recording	n.a.
f. Other	

E. Oth

SECTORS AND SUB-SECTORS	CORRESPONDING CPC Section B
CONSTRUCTION AND RELATED ENGINEERING SERVICES	
A. General construction work for buildings	512
B. General construction work for civil engineering	513
C. Installation and assembly work	514+516
D. Building completion and finishing work	517
E. Other	511+515+518
DISTRIBUTION SERVICES	
A. Commission agents' services	621
B. Wholesale trade services	622
C. Retailing services	631+632 6111+6113+6121
D. Franchising	8929
E. Other	
EDUCATIONAL SERVICES	
A. Primary education services	921
B. Secondary education services	922
C. Higher education services	923
D. Adult education	924
E. Other education services	929
ENVIRONMENTAL SERVICES	
A. Sewage services	9401
B. Refuse disposal services	9402
C. Sanitation and similar services	9403
D. Other	
FINANCIAL SERVICES	
A. All insurance and insurance-related services	812**
a. Life, accident and health insurance services	8121
b. Non-life insurance services	8129
c. Reinsurance and retrocession	81299
d. Services auxiliary to insurance (including broking and agency services)	8140
B. Banking and other financial services (excluding insurance)	
a. Acceptance of deposits and other repayable funds from the public	81115-81119
b. Lending of all types, including consumer credit, mortgage credit, factoring and financing of commercial transaction	8113
c. Financial leasing	8112
d. All payment and money transmission services	81339**
e. Guarantees and commitments	81199**
f. Trading for own account or for account of customers, whether on an exchange, in an over-the-counter market or otherwise, the following:	
- money market instruments (cheques, bills, certificates of deposits, etc.)	81339**
- foreign exchange	81333
- derivative products including, but not limited to, futures and options	81339**
- exchange rate and interest rate instruments, including products such as swaps, forward rate agreements, etc.	81339**
- transferable securities	81321*
- other negotiable instruments and financial assets, including bullion	81339**
g. Participation in issues of all kinds of securities, including underwriting and placement as agent (whether publicly or privately) and provision of service related to such issues	8132

S AND SUB-SECTORS	CORRESPONDING CPC Section B
j. Settlement and clearing services for financial assets, including securities, derivative products, and other negotiable instruments	81339** or 81319**
k. Advisory and other auxiliary financial services on all the activities listed in Article 1B of MTN.TNC/W/50, including credit reference and analysis, investment and portfolio research and advice, advice on acquisitions and on corporate restructuring and strategy	8131 or 8133
l. Provision and transfer of financial information, and financial data processing and related software by providers of other financial services	8131
Other	
ALTH-RELATED AND SOCIAL SERVICES her than those listed under 1.A.h-j.)	
Hospital services	
Other human health services	9311
	9319 (other than 93191)
Social services	
Other	933
URISM AND TRAVEL-RELATED SERVICES	
Hotels and restaurants (including catering)	
Travel agencies and tour operators services	641-643
Tourist guides services	7471
Other	7472
CREATIONAL, CULTURAL AND SPORTING SERVICES er than audiovisual services)	
Entertainment services (including theatre, live bands and circus services)	9619
News agency services	962
Libraries, archives, museums and other cultural services	963
Sporting and other recreational services	964
Other	
NSPORT SERVICES	
Maritime transport services	
a. Passenger transportation	
b. Freight transportation	7211
c. Rental of vessels with crew	7212
d. Maintenance and repair of vessels	7213
e. Pushing and towing services	8868**
f. Supporting services for maritime transport	7214
	745**
Internal waterways transport	
a. Passenger transportation	
b. Freight transportation	7221
c. Rental of vessels with crew	7222
d. Maintenance and repair of vessels	7223
Pushing and towing services	8868**
Supporting services for internal waterway transport	7224
	745**
ir transport services	
Passenger transportation	
Freight transportation	731
Rental of aircraft with crew	732
Maintenance and repair of aircraft	734

SECTORS AND SUB-SECTORS	CORRESPONDING CPC Section B
E. Rail transport services	
a. Passenger transportation	7111
b. Freight transportation	7112
c. Pushing and towing services	7113
d. Maintenance and repair of rail transport equipment	8868**
e. Supporting services for rail transport services	743
F. Road transport services	
a. Passenger transportation	7121+7122
b. Freight transportation	7123
c. Rental of commercial vehicles with operator	7124
d. Maintenance and repair of road transport equipment	6112+8867
e. Supporting services for road transport services	744
G. Pipeline transport	
a. Transportation of fuels	7131
b. Transportation of other goods	7139
H. Services auxiliary to all modes of transport	
a. Cargo-handling services	741
b. Storage and warehouse services	742
c. Freight transport agency services	748
d. Other	749
I. Other transport services	
12. OTHER SERVICES NOT INCLUDED ELSEWHERE	95+97+98+99

The (*) indicates that the service specified is a component of a more aggregated CPC item specified elsewhere in this classificat list.

The (**) indicates that the service specified constitutes only a part of the total range of activities covered by the CPC concorda (e.g. voice mail is only a component of CPC item 7523).

ANNEXURE-V

SERVICES PROPOSED TO BE EXEMPTED

Sr. No. as per WTO	Sector		Sub-sectors/Services
1.	**Business Services**	**B**	**Computer & related services**
		a	Consultancy services related to the installation of computer hardware
		b	Software implementation services
		c	Data processing services
		d	Database services
		e	Other
		C	**Research & Development Services**
		a	R & D services on natural sciences
		b	R & D services on social sciences and humanities
		c	Interdisciplinary R & D services
		F	**Other business services**
		f	Services incidental to agriculture and forestry
		g	Services incidental to fishing
2	**Communication Services**	**A**	**Postal Services**
			Post Cards
			Money Orders
		D	**Audiovisual Services**
		b	Motion picture projection service (Theatres)
3	**Construction & related Engineering Services**		Rural Housing
			Slum Development
			Lower & Middle Income Group Housing
5	**Educational Services**	**D**	**Adult education**
7	**Financial Services**	**A**	**All insurance and insurance-related services**
		a	Life, accident and health insurance services, crop insurance

		B	**Banking and other financial services (excluding insurance)**
		a	Acceptance of deposits and other repayable funds from the public
		b	Lending of all types, including consumer credit, mortgage credit, factoring and financing of commercial transaction.
10	**Recreational, Cultural and sporting Services (other than Audiovisual services)**	**A**	**Entertainment services (including theatre, live bands and circus services)**
		C	**Libraries, archives, museums & other Cultural services**
		D	**Sporting and other recreational services**
11	**Transport services**	**B**	**Internal waterways transport**
		a	Passenger transportation
		b	Freight transportation
		c	Rental of vessels with crew
		d	Maintenance and repair of vessels
		e	Pushing and towing services
		f	Supporting services for internal waterway transport
		D	**Space Transport**

ANNEXURE-VI

Segment	Segment growth rates assumed	Potential tax base 1999-2000 (Rs. in Crores)
Key Sectors		
Transport and Storage		
Land Transport		
Railways	NA	31,575
Land Transport-public transport by buses	9.7%	12,674
Pipelines-HBJ revenues to GAIL	0.0%	1,120
Water Transport		
Coastal and offshore	2.0%	455
Major ports	13.8%	3,802
Air Transport	NA	297
Services incidental to transport	NA	
Storage and Warehousing	9.1%	546
Post and Telecommunications		
Post		
Postal services	1.9%	1,284
Telegraph services	-04.0%	58
Telecommunications		
Internet Service Providers	NA	102
Cable Operators	NA	52
Banking & Financial Institutions		
Banks	14.6%	9,433
Financial Institutions	21.3%	866
Other Sectors		
Construction	NA	
Hotels and Restaurants	NA	2,383
Business services	NA	
Education	NA	1,000
Health and Medical services	NA	
Media	12.0%	3,210
TOTAL		**68,857**