

# **HOTEL ASSOCIATION OF INDIA**

## **PRE-BUDGET MEMORANDUM 2008-09**

The tourism sector in India is making a major contribution in the growth of national economy. For the fourth consecutive year in 2006, the sector recorded a double digit growth in the number of foreign tourist arrivals and foreign exchange earnings. As per published statistics of the Ministry of Tourism, 4.43 million International tourists visited India in 2006. The foreign exchange revenue earned from foreign tourists in 2006 was US\$ 6569 million, i.e. Rs. 29604 crores which is about 1% of GDP. The resultant number of direct and indirect jobs created by the tourism sector have been estimated at 41.8 million by the Ministry of Tourism.

The World Travel and Tourism Council (WTTC) has identified India as one of the foremost growth centers in the World in the coming decade. The advent of low cost domestic carriers and huge investments being made to develop 35 non-metro airports and new greenfield airports will stimulate the growth of new tourism destinations, and of hospitality infrastructure.

The need of the hour is therefore to ensure that the growth momentum achieved by Indian tourism sector is maintained, sustained and carried forward. To achieve this objective, the following incentives for growth of hotel industry may be included in the Union Budget 2008-09.

### **Direct Taxes**

#### **1. Section 80 IA : Infrastructure Status for Hotel Industry**

With the sharp spurt in business and leisure travelers to India, the country is currently experiencing a shortage of almost 100000 hotel rooms to meet the accommodation needs of the foreign and

domestic tourists. The hotel industry is a highly capital intensive industry. Construction of a new hotel project in 5 Star category demands massive Capital Investment ranging from Rs. 300 to Rs. 500 crores. The bulk of investment in a hotel is on land and building which has a very long period of return on investment to the investors.

To accelerate the pace of construction of more hotel rooms, the hotel industry therefore needs to be declared an infrastructure industry under Section 80 I/A of the Income Tax Act 1961. It should be given full benefits of concession for infrastructure facilities available to other sectors like airports, seaports, power projects and gas distribution networks.

In the Union Budget 2007-08 tax holiday of 5 years for Two-Star, Three-Star, Four-Star Hotels and Convention Centers with a seating capacity of not less than 3000 in the NCR area of Delhi, Faridabad, Gurgaon and Gautam Budh Vihar, Ghaziabad was given to speed up the infrastructure of hotel rooms needed for the Commonwealth Games in 2010. This facility needs to be extended to hotels of all categories across the country in the forthcoming Union Budget. It would give a boost to the growth of hotel accommodation in the country.

The faster construction and availability of adequate additional hotel room capacity would result in doubling of foreign tourist arrivals from 4.43 million tourists in 2006 to about 10 million tourists by 2010. This in turn could result in doubling of foreign exchange earnings from tourism i.e., from Rs. 30,000 crore in 2006 to Rs. 60,000 by 2010 and increase tourism's contribution to GDP from 1% to 2% as also enlarge the employment opportunities in the country.

## **2. Section 72 A- Amalgamation and Mergers**

Section 72 A of the IT Act, has been amended to include the hotel industry under its ambit to set off of accumulated losses and depreciation on amalgamation to help the loss making hotel companies.

As per the amended section, an amalgamated company is allowed to carry forward and set-off of losses on the fulfillment of the conditions that :-

- (i) It has been engaged in the business for at least three years during which the accumulated business loss was incurred or the unabsorbed depreciation was accumulated.
- (ii) As on the date of amalgamation, it has continuously held at least three-fourths of the book value of fixed assets, which are held by it two years prior to the date of amalgamation;
- (iii) Three-fourths of the book value assets of the amalgamating Co. be held for at least five years;
- (iv) Continues same business as that of amalgamating Co. for at least five years;
- (v) Production level of at least fifty per cent of the installed capacity of amalgamating Co. to be achieved.

To enable hotels to draw the benefits u/s 72/A, it is recommended that:-

- (i) The continuity to hold assets of the amalgamating Co. should be confined to 50% of the book value in order to make the amalgamation viable so that recycling is possible and assets are procured in order to keep up with latest technology.
- (ii) Continuance of business of amalgamating companies should be reduced from five years to two years to facilitate effective re-organisation.

- (iii) Achieving installed capacity may not be possible for the service sector companies, which are given the benefit under this section, hence, this condition should not be made applicable to service sector companies.

### **3. Section 32 - Depreciation on Hotel Buildings**

Hotels were eligible for the depreciation allowance of 20% on their plant (building) till 31<sup>st</sup> March 2002. The depreciation allowance for hotels was, however, scaled down to 10% vide Notification No. 291/2002 dated 27.09.2002.

Hotel buildings constitute the '*plants*' for the hotel industry as their usage is round the clock for 24 hours. The industry has to make very heavy investments in renovation, upgradation and upkeep of the hotel buildings. Section 32 of the IT Act should therefore be amended to restore the depreciation rate to 20%. The additional depreciation applicable to Plant & Machinery u/s 32 1 (ii a) should also be allowed to hotels which have to make heavy investments in plant and machinery.

### **4. Chapter XII H of IT Act. - Fringe Benefit Tax**

Business related expenses like telephone, sales promotion, etc. have been brought in the ambit of Fringe Benefit Tax (FBT). Meals provided in office are exempt but if there is reimbursement for the same then it gets covered, which is leading to contradictory situation. Contributions to approved superannuation funds are also being made applicable under the FBT, even in the case of loss making companies.

It is therefore, recommended that the contributions to superannuation funds should be removed from the purview of this provision for the following reasons :-

- (i) Existing superannuation schemes would become unviable in future;
- (ii) The effective tax to be borne by Corporates would be more than 40%, since FBT is not tax deductible;
- (iii) Employee receiving his pension from the fund would be paying his regular tax on the same;
- (iv) It should not be made applicable to loss making companies, which primarily do not pay any base tax.

#### **5. Section 115 (O) - Dividend Distribution Tax**

The effective rate of the Dividend Distribution Tax is 16.995% inclusive of surcharge and education cess. It is recommended that this section be deleted as it results in double taxation.

#### **6. Section 115 (J) - Minimum Alternative Tax (MAIT)**

The Minimum Alternative Income Tax (MAIT) was introduced in 1997 on the Companies. The hotel industry has been recognized as Service Export industry and is entitled to all the export benefits under the Foreign Trade Policy announced every year by the Ministry of Commerce. Since exporters are exempt from Section 115 (J), it is requested that the hotel industry should also be exempted from MAIT.

#### **7. Income Tax – Section 194 I (TDS)**

Payment made to hotels are not the payment of rent, per se and hence Hotels should be excluded from the purview of Section 194I for the purpose of Tax Deduction at Source. CBDT may issue appropriate circular in this regard.

#### **8. CVD on Imported Liquor**

The Ministry of Finance (Deptt. of Revenue) vide its Notification No. 82/2007-CUS dated 3.07.2007 has withdrawn the Countervailing Duty (CVD) on Imported Liquor. As per newspaper reports, it appears that Central Government may introduce a bill in Parliament to authorize State Governments to levy excise duty on imported liquor. Such a move would be counter productive and tourism unfriendly.

Under the “Served from India Scheme” hotels are entitled to set off the CVD against their entitlement of Duty Credit Scrips upto 5% of their foreign exchange earnings. As a result of above incentive to hotels, on an average, prices of imported liquor have come down by 25% - 35% across the various categories of wines and spirits from the peak 2003 levels. This has greatly enhanced India’s credibility as a tourist friendly and affordable destination country. Authorising the State Governments to levy a duty equivalent to the CVD by the State Governments would therefore seriously undermine the capability of hotels in India to remain competitive with the hotels in competing open market countries like Singapore. It is therefore submitted that the State Governments should not be empowered to Levy excise duties on imported liquor which would give rise to manifold problems. Rather, it would be appropriate to utilize the current situation as an opportunity to revamp the current regulatory excise regime on spirits and wine and standardize it across all the States in India which would be tourist friendly, convenient to administer and beneficial in more ways than one.

## **Indirect Taxes**

### **(1) Service Tax**

- (i) Hotels are required to pay Service Tax on services received outside the territory of India, specially commission paid to Foreign Travel Agents. Hotel industry is one of the prime foreign exchange earners and is recognized as a service export industry. It is therefore recommended that hotels should be exempted from

paying service tax on services received from Foreign Tour Operators.

- (ii) Under the existing provisions, Banquet (Outdoor as well as indoor catering) Guests are charged both the Service Tax on Food & Beverage and VAT. This tantamounts to double taxation for the guests. It is therefore recommended that only VAT be charged on Food & Beverage and provision regarding Service Tax in Banquet Catering be deleted.

**(2) Deemed Exports to be Exempted from Terminal Excise Duty**

Under the existing provisions, the Central Excise Duty is first paid to the Department of Revenue (Excise Range) and is then refunded by the Ministry of Commerce (Regional Licensing Authority). The procedure is cumbersome and of no advantage to the Government. It is therefore recommended that excise duty on deemed exports be exempted.

**(3) VAT**

Presently, VAT is not levied on the products procured for export purposes. It is, however, levied on capital equipment procured from domestic sources under EPCG scheme or against Duty Credit Scalp. Since VAT is also not levied on direct imports, it is recommended that it should also be exempted on items sourced indigenously against invalidation letter issued under EPCG Scheme in lieu of direct import.

**(4) Central Excise**

Hotels are subject to the applicability of central excise on confectionery items like cakes, pastries and chocolates. As this is not the core business of the hotels, it does not result in a substantial contribution to the central revenues. On the other

hand, the documentation required to be maintained by hotels for this purpose is disproportionate to the meager realization of excise revenue. Hotels should therefore be exempted from the applicability of central excise on confectionery.

**(5) CENVAT Credit**

Hotels have to sometimes procure capital equipment from domestic sources against Duty Credit Scrap under the Served From India Scheme. Since the full excise duty is already debited in the Duty Credit Scrap issued under the Served From India Scheme, the domestic supplier/ manufacturer should have the option to get the benefit of CENVAT Credit.

**(6) Special Entry Tax (Octroi)**

Some States levy Special Entry Tax on all Capital Goods purchased from outside that State. In view of implementation of State VAT across most of the States, it is submitted that Special Entry tax should not be levied.

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