

For heaven's sake, please scrap FBT! – Feb 13, 2008

THAT Fringe Benefit Tax, which was introduced by Mr PC in the 2005-06 Budget, is a highly successful revenue earner hardly needs to be over emphasized. Look at what FBT is bringing into the Government's coffers..... FBT has raked in revenue to the tune of Rs 5,121 crores during the period April 1007 to January 15, 2008, as against a total collection of only Rs 3,108 crores during the corresponding period of 2006-07, reflecting a growth rate of about 65%. Considering the fact that most of the FBT element on ESOPs would get paid in the last quarter of 2007-08, one can see a significant improvement in the FBT collections, justifying its position as a major revenue earner for the Government.

But, can the simple fact that the Government is raking in significant revenues thro FBT justify this very levy?

FBT was introduced in the 2005-06 Budget with the intention of taxing the perquisites or fringe benefits provided by an employer to his employees, in addition to the cash salary or wages paid and certain expenditures of companies like the ones on sales promotion and use of telephone among others. This was what Mr PC had to say, in Para 160 of his 2005-06 Budget speech :

“I have looked into the present system of taxing perquisites and I have found that many perquisites are disguised as fringe benefits, and escape tax. Neither the employer nor the employee pays any tax on these benefits, which are certainly of considerable material value. At present, where the benefits are fully attributable to the employee they are taxed in the hands of the employee; that position will continue. In addition, I now propose that where the benefits are usually enjoyed collectively by the employees and cannot be attributed to individual employees, they shall be taxed in the hands of the employer. However, transport services for workers and staff and canteen services in an office or factory will be outside the tax net. The tax is not a new tax, although I am obliged to call it by a new name, namely, Fringe Benefits Tax. The rate will be 30 per cent on an appropriately defined base.”

The subsequent actions of the FM and his Ministry don't seem to justify the 'honourable' intentions with which the levy was first introduced. Can anybody dispute the fact that FBT does tax a Company on its highly legitimate business expenses like sales promotion, business travel, usage of telephones, etc. which per se, have nothing to do with its employees? How on earth can anybody say that an employee gains by going on a business travel? On the other hand, not only does an employee suffer by traveling, even his family suffers.

FBT, being a presumptive tax seeks to tax even loss-making corporates, making it very unfair and unjust. Even companies which have no prospect of making profits for many years to come,

are still required to pay FBT. Is this not obnoxious and does this not go against the very concept of a direct tax which can be paid by somebody only when he makes profits?

As a concept, FBT like any tax is supposed to affect something which was not being taxed before its introduction, as per any logical and ethical reasoning. Right. Take the case of FBT payable on medical reimbursement to employees, which is exempt to the extent of Rs 15,000/- in a year in the hands of the employee. Now, after the introduction of FBT, the same medical reimbursement given to employees attracts FBT in the hands of the employer. With nothing new happening, on the same expenditure, the Company pays FBT. Does this have any logic?

Another area of concern is that, FBT requires extensive and highly complicated documentation. Many of our clients in the IT sector have had to deploy extra personnel just to be able to track the various heads of expenses which attract FBT. For corporates who work on the Cost To Company ('CTC') logic, the levy of FBT has meant that the concerned employee takes lesser take home pay, after the introduction of the FBT, on the same salary component, as many employees follow the policy of adding up all outflows as part of the CTC on their employees.

Another argument against FBT is that, even the Ministry and the CBDT have not been able to fully comprehend its various implications. A 40-page explanatory circular issued by the CBDT in August 2005 is proof of complexity behind this levy. Take the recent case of the introduction of FBT on ESOPs. After the 2007-08 Budget wherein Mr PC had announced that ESOPs would get covered by FBT, it took CBDT six long months to come out with the Valuation Rules in October 2007, only to issue a clarificatory circular containing FAQs on ESOPs, on December 20, 2007. The fact that even the CBDT seems to be confused about the levy does not speak highly of this complex levy. (It is another matter that the very concept of levying FBT on ESOPs especially, in respect of foreign shares, is obnoxious if not illegal, as I had pointed out in my earlier piece on TIOL).

Another major grudge that I have against this levy is that, it discriminates tax payers. Any discrimination on the basis of an incentive given by the Government is justifiable. But, to discriminate tax payers on the basis of whether they belong to the software sector or the construction industry or the pharma industry is clearly obnoxious and unconstitutional. How can anybody justify levy of FBT on a lower base of only 5% for the computer software, construction and pharma sectors, while other corporates are required to pay FBT on a higher base of 20%. For that matter, how can anybody justify the fact that computer software industry is treated more favorably as compared to its very poor cousin, the BPO industry. Where was the justification to allow the software industry to pay FBT on a much lower base of 5% of the traveling expenses for the whole of 2005-06, while everybody else had to pay FBT on the higher base of 20%. How does Mr PC explain his love for the software industry, or the lack of it for the

rest of the players?

One latest trend has been that, the FBT logic is being used to reduce the overall tax payments to the Government. Many corporates are known to have devised legally sustainable 'FBT friendly' elements forming part of the pay structure of their senior employees, wherein, corporates pay minimal FBT on these items allowing the employees concerned to save on payment of income tax which they would otherwise have paid. On the face of it, nothing seems illegal in this methodology, except for the fact that the Government seems to be the loser. For, while the Government would indeed be collecting FBT on these items of expenditure of corporates, the employees would have saved payment of personal income tax at the maximum rates, resulting in a net loss of revenue to the Government.

My learned friend, Kirit Sanghvi, the Mumbai based CA, an authority on the subject, would talk of the FBT systems that prevail in various countries of the world, in his authoritative book on FBT published by Show White. Both the US and the UK have not gone in for FBT. Some of the very few countries that have gone in for FBT include Australia and New Zealand. I believe that Australia is also looking at ways and means of reducing the overall reach of FBT, whose impact is in any case, rather low, on its corporate sector.

The only logic then, in continuing FBT seems to be its contribution to the Government coffers. The corporate sector contributes corporate income tax to the tune of about Rs 170,000 crores to the Government and would have no qualms if the FM would increase the rate of corporate income tax by say, two percentage points or go in for an increase in the 'Minimum Alternate Tax ('MAT') rates, in order to compensate for the loss of revenue to the Government. After all, nobody disputes the logic behind the levy of MAT on corporates, which is fully justified and a rise in the MAT rates coupled with an increase in tax rates to meet revenue targets should be fine. What bothers the corporate sector is the fact that FBT, though constituting less than 5% of the direct taxes collected in the country, makes its life more difficult and complicated by at least five times. Perhaps, there is no need even to look at an increase in the tax rates. Removal of FBT will release a lot of productive energy to the corporate sector, which it can use, more productively, to earn more revenues and consequently, pay more taxes.

It was the great Chanakya who declared that taxation should be a painful process for the people. While he has also talked about the quantum of tax which can be collected by a government, he has repeatedly stated that the process of tax collection should be simple and not complicated. Viewed in the light of what Chanakya said, FBT as a levy miserably fails, because, more than anything else, of its complexity. The working logic in both the IT Department as well as with the corporates seems to be that, whatever expense which is not a perquisite, should be treated as FBT related. Surely, in independent India, no other levy would

seem to have been so complex and obnoxious.

An otherwise brilliant economist and lawyer and an astute politician, Mr PC would seem to have become quite unpopular on account of the FBT levy. I've been an admirer Mr PC and would hate to see his image getting tarnished on account of the FBT levy which has remained a major irritant. With the tax revenues continuing to rise impressively, it is perhaps time for Mr PC to dump FBT and regain his popularity.

Is the FM listening?

P.S. It is very rare that I use the word 'obnoxious'. I have repeatedly used this word in this piece, perhaps, due to the lack of the knowledge of the existence of a more appropriate word which would characterize FBT.