



Indian clients to feel pinch of new tax on law firms, LPOs

By Rashida Yosufzai | Thursday, 9 July 2009

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Amid growing opposition and unrest in India's legal community, Indian law firms' fee income will be taxed as part of the government's annual budget changes.

Finance Minister Pranab Mukherjee defended the decision to charge all law firms and consultancies a 10.3% tax on services in his budget speech. "Although there is a school of thought that legal consultants do not provide any 'service' to their clients, I hold my distinguished predecessor in high esteem and disagree," he said. "As such, I propose to extend service tax on advice, consultancy or technical assistance provided in the field of law."



India's legal community has argued that the law is not a business like other trades and therefore should not be taxed. Legal bodies have organised a lawyers strike on 9 July in protest. "The lawyers of India will not tolerate any attempt by the government to impose service tax on the legal fraternity and shall adopt all peaceful means to oppose such uncalled for and unwarranted taxes on lawyers," said a statement issued by the Co-Ordination Committee of All Bar Associations of Delhi, the organiser of the strike.

Lawyers also argue that the tax costs will inevitably be passed on to clients, further preventing people from seeking legal advice and thus curbing growth of the country's developing legal industry. "The legal industry here has grown to a great extent," said N Raja Sujith, partner at Majmudar & Co. "Instead of offering perks or tax exemptions to support that growth, this tax has been imposed and is not ideal. In India most of the mid-level companies and businesses don't seek proper legal advice as it is, because of the costs. That is somewhat changing now, and law firms are doing better. With this burden, clients will have to pay more, so obviously they will think twice and avoid legal services."

Rajasujit added that local clients are more likely to be affected by the surcharge due to exemptions on foreign clients. "This will mean basically a 10% tax on each bill we raise, and it's going to affect the local Indian clients more than foreign clients because there may be exemptions if it's an exported service."

The tax also contains various other loopholes-exemptions apply if legal services are being offered by individuals, to other individuals. As such, smaller law firms in India—which constitute the majority of the country's legal industry—may be able to bypass the tax. "Most firms are small and unregistered, and they can always charge their bills individually under each partner's name. The receiver will also suggest that, to prevent them paying the extra service tax. Through that loophole, some firms can avoid the tax so I don't know how the authorities will be able to monitor that. There is a huge scope of issues at this stage where people may interpret things differently."

Despite the opposition, Rajasujit said that there is a strong likelihood of the move being approved by parliament, and may come into effect as soon as 1 August. "This issue has been discussed over the last three years in past finance budgets," he said. "I feel that it will come into effect. Unless the legal fraternity can influence the parliament, it will most probably be approved."

Nishith Desai, the founder of Nishith Desai Associates agreed. "More likely than not it will be approved by parliament, but of course, one cannot rule out the possibility of legal challenges," he said. "Legal services were one of the few major services that were left out of the service tax net initially and it was only a matter of time before it was also included, especially considering the revenue that it can generate."

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