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Businesses, small taxpayers to gain from new direct tax code

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Livemint, New Delhi



The new tax code, which will replace the Income Tax Act of 1961, is expected to overhaul the taxation system.(Mint file photo)

Businesses and small personal income tax payers are set to emerge as big gainers from the new direct tax code the government is working on.

The proposed code, the draft of which will be ready by July, will take forward the unfinished agenda of lowering corporate tax rate to 25% for all businesses and seek to give further relief to personal income tax payers in lower slabs.

The idea is to moderate tax rates for these assesseees without squandering the recent gains in revenue growth and tax base. Therefore, tax rate cuts will be incremental over a period of time as compliance and revenue collections grow. Between fiscal 2014 and fiscal 2018, income tax returns filed have gone up by over 80% to 68.4 million.

The highest personal tax slab of 30% for individuals, will, however, stay at current level in the new code as it is considered among the lowest in the world, while smaller taxpayers will get relief, a person familiar with the discussions on the code said on condition of anonymity. Relief to small taxpayers could fetch the ruling NDA government electoral gains as the country goes to polls next year.

The intention to make the industry more competitive with a lower 25% tax rate does not mean personal income earners in the highest slab of 30% as a class of taxpayers will be at a disadvantage. Dividend distribution tax will make sure the tax burden on income that shareholders of companies take out for consumption—already taxed at the applicable corporate tax rate—is higher than the tax burden on personal income taxpayers in the highest slab, explained a second person privy to discussions on the code, who also spoke on condition of anonymity.

“In most advanced economies, individuals are taxed at a higher rate than companies to promote investments and job creation,” said Amit Maheshwari, partner, Ashok Maheshwary and Associates LLP.

The benefit of a lower 25% corporate tax first offered to companies with annual revenue less than Rs50 crore in the 2017-18 budget, was extended to businesses with sales up to Rs250 crore a year in 2018-19. The direct tax code will spell out the roadmap for eventually extending this lower rate to all companies in line with revenue growth. Reducing corporate tax to make the industry more competitive has become a policy priority as many nations including the US and UK are wooing investments with reduced tax rates.

The code will seek to further reduce tax evasion and improve compliance so that the ratio of direct taxes to gross domestic product (GDP) goes up from the present level—5.9% in fiscal 2018 and a projected 6.1% in the current fiscal year—to at least 9% in the short term. There could be room for further improvement on this count eventually as the tax-to-GDP ratio of comparable economies (including state taxes) is about 24%, roughly half of which should be from direct taxes, said the first person quoted above.

The two structural changes in recent years—demonetization in November 2016 and rollout of the goods and service tax (GST) in July 2017—have helped the government increase the number of direct tax payers. With the increased cross references between the tax return filings of both GST and corporate taxes, revenue understatement is set to become difficult for businesses.

Taxation of digital economy, reducing frivolous litigation and making the corporate tax rate more competitive are expected to be the focus areas of the new tax code, said Girish Vanvari, founder of advisory firm Transaction Square.

“Industry is also looking for certainty so that it can plan five years ahead. For instance, the 25% rate for industry was announced but it still comes with many riders and keeps out many companies,” said Riaz Thingna, director, Grant Thornton Advisory Pvt Ltd.

The new tax code, which will replace the Income Tax Act of 1961, is expected to see an overhaul of the legal provisions including concepts of what constitutes income and scope of taxation. “It is a myth that jurisprudence will be unsettled by an overhaul of the Income Tax Act. In fact, it will enable putting the jurisprudence as pronounced by the courts into the statute book for the benefit of everyone,” said the first person cited earlier.

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