

Amendment to income tax act

September 27, 2019

Source: *The Hindu*

Manifest pedagogy: Corporate tax rates are a key parameter guiding investments vis-s-vis other emerging markets. Moreover, due to the ongoing trade tensions with respect to USA and China, many companies are finding suitable places to invest abroad. In this regard, review of tax cuts are important to boost competitiveness, make in India and also create a virtuous cycle of domestic investments and growth.

In news: Income tax act has been amended and corporate tax has been cut

Placing it in syllabus: Changes in economic policies

Static dimensions:

- Corporate tax in india and other developing countries
- Corporate tax cut
- Slowdown in the economy
- A virtuous cycle of investment

Current dimensions:

- Key changes
- Potential impact

Content:

Income tax and Corporate tax in India and other developing countries:

Corporate tax is a tax imposed on the net income of the company. Companies, both private and public which are registered in India under the Companies Act 1956, are liable to pay corporate tax.

India's corporate tax rate (before rate cuts) was among the highest in South Asia and ASEAN, making it uncompetitive when it comes to attracting foreign investments. With base tax rate coming down to 22 per cent (15 per cent in case of new investments in manufacturing), the country now has one of the lowest corporate tax rates in the region.

Singapore with 17 per cent tax rate, and Vietnam, Thailand, Cambodia and Taiwan with 20 per cent base tax rates are the only countries offering lower rates than India.



For long, Vietnam has been considered a big threat to India as it has successfully been attracting foreign investors through lower tax rates. Lot of manufacturers leaving China because of Sino-US trade disputes are said to be opening shops in Vietnam with lower tax rates being one of the reasons for investors' preference for the country.

The move makes India attractive from a tax perspective. A report released by Kotak Economic Research said that the revised rate will be attractive for companies looking to shift from China or considering a China plus one policy.

India has removed the tax disadvantage for companies looking to set up capacity in India.

Corporate tax cut:

- The corporate tax rate has been **reduced from 30 per cent to 22 per cent** with effect from 2019-20.
- Any domestic company will have the option to pay income tax at the rate of 22 per cent (plus surcharge and cess; effective tax rate at 25.6 per cent) subject to the condition that **they will not avail any exemption/incentive.**
- Such companies would **not be required to pay Minimum Alternate Tax (MAT).**

- Domestic Manufacturing companies set up after October, 2019 to get option to pay 15% tax (effective tax rate at 17.01 per cent).
- This benefit is available to companies that do not avail of any exemption/incentive and commence their production on or before March 31, 2023. These companies will also not be required to pay MAT.
- For listed companies that have announced buyback before July 5, 2019, tax on buyback of shares will not be charged.
- Enhanced surcharge will not apply to capital gains arising on equity sale or equity-oriented funds liable to Security Transaction Tax (STT).

The revenue foregone for this move will be Rs 1.45 lakh crore annually.

Tax rates and slowdown in the economy:

The general trend around the world has been to bring down the burden of corporate tax. The revenue from corporate tax was 3.56% of GDP in India for 2018-19. The share of direct taxes, including personal income tax, was 6.4% of GDP. Regressive indirect taxes still account for more than 60% of all tax collections in India, including by the states.

However, corporate tax is non-transferable only in a formal sense. Companies calibrate their pricing to take into account a high rate of corporate tax, thereby passing on the burden to the consumer. The only way this can be prevented is if the market is very competitive.

Therefore, it makes sense to have low, uniform rates of import duty, and low rates of corporate tax comparable to those in similarly placed economies. However for the tax cuts to suffice to reverse the ongoing economic slowdown calls for **sustained investment.**

To achieve a sustained boom, investment in infrastructure must

pick up. For this to happen the **broken financial mediation mechanism** has to be fixed – banks burdened by bad loans, tottering non-banking financial companies (NBFCs) and a dysfunctional debt market and a healthy model of public-private-partnership (PPP) in big projects.

A virtuous cycle of investment:

The economic survey 2018-19 has found the **investment as the “key driver” that can create a self-sustaining virtuous cycle** in India. This investment can be both government investments in infrastructure, as well as private investments.

The Survey said the economy was always on disequilibrium – either on a virtuous or a vicious cycle. **When the economy is in a virtuous cycle, investment, productivity growth, job creation, demand and exports feed into each other and enable it to thrive.**

Especially private investment, is the “key driver” that drives demand, creates capacity, increases labour productivity, introduces new technology, allows creative destruction, and generates jobs. Capital investment fosters job creation, as capital goods production, research & development, and supply chains also generate jobs.

However, investment is risky entrepreneurs are exposed to the risk of business failure that leads to the loss of the invested capital. Therefore, savings have to increase more than investment to allow for the accumulation of precautionary savings.



The survey also finds that exports must form an integral part of the growth model because higher savings preclude domestic consumption as the driver of final demand. Domestic consumption can act as a force-multiplier when high income growth feeds consumption.

However, as currently the global market is extremely competitive, with the firms that are able to produce at the lowest costs having the ability to gain market share in exports. So, average productivity of firms in the economy becomes crucial to export competitiveness. Capital investment enhances total factor productivity, which in turn enhances export performance.

Key changes in Income Tax Act:

- The government has introduced a new Section called **194N** in income tax laws under which **cash withdrawals exceeding ₹1 crore in aggregate in a year** from banks, post offices or co-operative society engaged in carrying on the business of banking will attract a TDS. **Payments made on or after September 1, 2019 will attract the provisions of Section 194N.**
- The government has **amended 194-IA of the Income Tax Act** to include all charges of the nature of club membership fee, car parking fee, electricity or water facility fee, or any other charges of similar nature, which are incidental to transfer of immovable property, for levy of TDS. TDS is **levied @ 1%** if the value of the **property exceeds ₹50 lakh.**
- New Section called **194M** has been introduced under which individual is required to deduct **TDS @5%** for paying a sum in excess of ₹50 lakh for carrying out any work in pursuance of a contract or by way of fees for professional services during a financial year.
- A higher **TDS of 5%**, (from 1% earlier) will be levied if life **insurance maturity proceeds** received that are taxable in one's hands.
- Those **who don't have PAN can quote Aadhaar in transactions** that otherwise require quoting of PAN like cash deposit above ₹50,000.

Impact of the new changes:

- Tax concessions will bring investments in Make in India, boost employment and economic activity.
- Promote investment and growth.
- Tax net will be widened which results in more revenue to the government.
- Will make Indian companies globally competitive and helps in arresting economic slowdown.
- Corporate tax cuts will cost the government Rs 1.45 lakh crore annually. This increases the chances of higher fiscal deficit and government may have to resort to spending cuts or embark on higher disinvestments.