No Gains For Taxpayers

Budget proposals on tax slabs and dispute resolution are unlikely to gain traction

Suranjali Tandon

AHEAD OF THE Union budget, taxpayers had anticipated a wide range of measures that they hoped would stoke demand. These ranged from lower tax rates to a more even tax structure on income from various sources. As the former was less feasible given the fiscal constraints, the budget proposals focused on simplification and providing ease to the taxpayer.

The recalibration of personal income tax slabs was suggested as a step towards simplification. However, its uptake is contingent on the preference for new slabs. Switching over to the new slab rates is not beneficial to an individual currently claiming full exemptions or with incomes comprising largely of capital gains. It is possible, however, that individuals do not claim such exemptions or deductions. An analysis of data published by Central Board of Direct Taxes suggests that for the assessment year 2018-19, if individuals do switch over to the new regime, it may translate to a 1 per cent improvement in tax collections, rather than a loss. It can be inferred that this option may be exercised by few individuals, if at all, since the potential gains from foregoing exemptions and the intended simplification is expected to be limited.

A common concern among taxpayers is protracted disputes. To reduce litigation, a new scheme has been proposed. My work on transfer pricing disputes reveals that 39 per cent of the cases made a reference to a similar case in the previous year. This underscores the importance of precedence. In such cases, settlement is not a superior option as the waiver of the penalty and interest does not offer any advantage against a decision that would impact future assessment. Further, the success rate of the tax department is 27 per cent at the Income Tax Appellate Tribunal (ITAT) and the Supreme Court and 12 per cent in appeals filed in high courts. Given the odds of success, an assessee may thus be tempted to pursue litigation. Thus taxpayers may choose to settle for the waiver of interest and penalty in cases where it is one time and does not set a precedent for future transactions.

The success rate of the tax department is 27 per cent at the Income Tax Appellate Tribunal ITAT and the Supreme Court and 12 per cent in appeals filed in High Courts. Given the odds of success, an assessee may thus be tempted to pursue litigation.

The other significant change is in taxation of dividends. The dividend distribution tax is a unique levy on distributed profits and is payable by the distributing company. The shortcoming of such tax is that foreign investors can't claim credit. Further, in an effort to make the tax progressive, an additional dividend tax of 10 per cent was introduced for domestic investors receiving dividend in excess of Rs 10 lakh. Changes in DDT were accompanied by a decline in dividend pay-out — the proportion of profits paid as dividends declined from 30 per cent in early 2000s to 22 per cent in 2019 (BSE 500 companies). It is expected that the reversion to the classical system may improve dividends payouts. However, this will benefit individual taxpayers with incomes below Rs 5 lakh as the slab rate applicable is less than the existing rate.

In the international arena, India is determined to tax cross-border incomes The addition of explanation 3A to the Income Tax Act reinforces India's commitment to taxing digital companies. The proposed amendment clarifies that incomes related to advertisement, sale of data of a person residing in India and sale of goods and services based on the data of a person residing in India, may be attributed to a business with nexus in India. Further, to tax Indian citizens that are not taxable in any other jurisdiction, the Act will now deem such individuals as resident taxable in India. While the application of the law may be challenged giving rise to disputes, it is a step forward.

The finance minister also referred to introducing a citizen's charter that incorporates taxpayer's rights and obligations. International experience shows that charters have limited enforceability unless adopted in primary legislation. Introducing it to the statutes may, therefore, prove to be a positive initiative. However, the devil lies in the detail. Faith can be built through enforcement of the charter. However, the penal provisions must be well-thought out so as to avoid adding another contentious element.

The budget proposals aimed to provide simplicity, yet much remains to be done, given the lack of uniformity in taxation of incomes such as capital gains. The success of schemes proposed is contingent on the traction they gain. As for the revenue implications, the impact of these measures may in fact be limited. Loss expected from lower tax rates may be countered by gains from the settlement of cases, higher dividend taxes on top incomes, and the wider scope for taxing international incomes.

The writer is assistant professor at NIPFP