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Impacts of Direct Tax Code on Individual Income: An Empirical Study

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ABSTRACT

The new code will completely overhaul the existing tax proposals for not only individual tax payers, but also corporate houses and foreign residents. It has been drawn with inspiration from the prevailing tax legislation in US, Canada and UK. It is a topic of interest and a matter of concern for every taxpayer in India. India wants to modernize its direct tax laws, mainly its income tax act which is now nearly 50 years old. The government wants a modern tax code in step with the needs of an economy which is now the third largest in Asia. The new tax code is expected to widen the tax base, end unnecessary exemptions, moderate tax rates and add to the government's coffers. In this paper, the researcher has attempted to study the impacts of The Direct Tax Code on Individual income by comparison of existing income tax Act and New Direct Tax Code.

Keywords : Direct Tax, Indirect Tax, Direct Tax Code, Individual Tax Payers

INTRODUCTION:

The Direct Tax code in India is very much discussed and criticized now –a- days. This Direct Tax Code is expected to be implemented from the financial year 2012 onwards. The DTC is expected to bring several changes in the very structure of Indian Direct Taxes. Some people are of the opinion that introduction of the DTC will defeat the very cannons of taxation as a result of which it will certainly affect both the individual as well as corporate tax players.

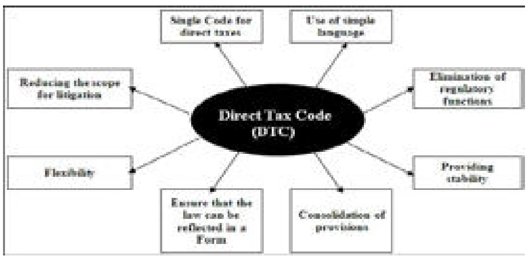
Recently the IT department of India put the new proposal for Direct Tax in front of Govt. of India and this is known as Direct Tax Code (DTC). The New Direct Tax Code (DTC) is said to replace the existing Income Tax Act of 1961 in India - and would be presented in the winter session of the Parliament. The aim of DTC is to make the current tax structure in India easy. Well, yes. This is the basic aim of DTC. India needs a new taxation system. An important part of the budget every year has been the detailing of the tax rates. However, with the introduction of the new direct tax code, the tax rates will not be part of the budget presented to Parliament every year.

MEANING OF DIRECT TAX CODE:

In Simple layman's language, there are basically two types of taxes - Direct and Indirect Direct tax is one which is taken by taking into consideration the individual characteristics of the tax payer such as Income tax, while Indirect tax means the tax which is levied by taking into consideration the number of transactions. Recently the IT department of India has put the new proposal for Direct Tax in front of Government of India and this is known as Direct Tax code (DTC).

SALIENT FEATURES OF PROPOSED DIRECT TAX CODE:

The salient features of the Code are as under:



OBJECTIVES OF THE STUDY

The main objectives of the study are as under:

1. To compare the new direct tax code with existing income tax Act – 1961
2. To evaluate the impacts of new direct tax code on individual income

IMPACTS OF DIRECT TAX CODE:

TAX RATE & INCOME SLAB:

DTC has redefined the Tax Slabs which will bring smile on the face of salaried class as Income tax exemption limit is now proposed at Rs2 lakh per annum, up from Rs1.6 lakh. Following tax slab has been proposed under the new direct tax regime.

(Table-1)

INCOME	TAX RATE
Up to Rs. 2,00,000	No tax
2,00,000 to 5,00,000	10% of the amount by which the total income exceeds Rs.2,00,000
5,00,000 to 10,00,000	Rs.30,000 + 20% of the amount by which the total income exceeds Rs.5,00,000
Above 10,00,000	Rs.1,30,000 + 30% of the amount by which the total income exceeds Rs.10,00,000

COMPARISION OF EXISTING TAX RATE AND PROPOSED TAX RATE:

The comparison of existing tax rate and proposed tax rate is as:

(Table-2)

INCOME SLAB	EXISTING RATE	PROPOSED RATE	NET CHANGE (%)
Up to Rs. 1,60,000	Nil	Nil	Nil
1,60,000 to 2,00,000	10%	Nil	10%
2,00,000 to 3,00,000	10%	10%	Nil
3,00,000 to 5,00,000	20%	10%	10%
5,00,000 to 10,00,000	30%	20%	10%
Above 10,00,000	30%	30%	Nil

SURCHARGE & CESS	EXISTING	PROPOSED
Surcharge	Nil	Nil
Cess	3%	Nil

In the proposed tax code though the threshold and rates will be retained, the slabs will be substantially liberalized, which would result in tax savings and increase in disposable income as shown in table-1. The direct tax code is a bit of a mixed bag for individuals, particularly the salaried class. Prima facie, the tax liability will reduce significantly as the draft code proposes to tax incomes up to Rs 5 lakh at 10%, that between 5 lakh to Rs 10 lakh at 20% and above Rs.10 lakh at 30%. (Refer Table-2).

TAX SAVINGS AT A GLANCE:
The tax saving as per the new direct tax code is as:

(Table-3)

Income	Current tax*	Proposed tax	Savings (Rs.)
Up to Rs. 1,60,000	Nil	Nil	Nil
1,60,000 to 2,00,000	4,120	Nil	4,120
2,00,000 to 3,00,000	14,420	10,000	4,420
3,00,000 to 5,00,000	55,620	30,000	25,620
5,00,000 to 10,00,000	2,10,120	1,30,000	80,120
Rs. 25,00,000	6,73,620	5,80,000	93,620

*Inclusive of 3% cess

INCOMES FROM EMPLOYER:
(Table-4)

Salary payments	Existing	Proposed	Impact
Basic salary	Taxable	Taxable	No impact
Wages	Taxable	Taxable	No impact
Annuity	Taxable	Taxable	No impact
Bonus	Taxable	Taxable	No impact
Commission	Taxable	Taxable	No impact
Leave encashment	Exempt	Taxable	Will increase taxable salary
Commuted pension and gratuity	Fully exempt for Government employees. Partially exempt for other employees.	Partially exempt for all employees provided amount is deposited in a 'Retirement Benefit Account' (RBA). Withdrawals from RBA will be taxed.	Will provide parity of treatment between Government and non-Government employees
Voluntary Retirement Compensation	Exempt upto Rs. 5 lakh, subject to specified conditions.	Exempt (subject to conditions to be specified) provided amount is deposited in RBA. Withdrawals from RBA will be taxed.	Conforms to EET principle

It is also proposed that all perks are to be considered part of the gross salary for the purpose of taxation. The bad news is that retirement savings will become taxable on withdrawal, as the draft code has proposed to usher in exempt-exempt-tax (EET) regime. The impact of that on tax liability of an individual will be known only when the rules are prescribed by the income-tax department at a later date.

But one thing is certain. The tax treatment of the perks enjoyed by the government employee and the private sector employee will be the same. The objective according to the draft code is to improve both the horizontal and vertical equity of the tax system across employees in all sectors. It has also proposed that benefits such as gratuity payment made to employees on change of jobs will be allowed tax exemption only if it is invested in a retirement fund. If an employee fails to invest it in such a fund, such receipts will be taxed at the appropriate marginal rate of tax.

PERMISSIBLE DEDUCTIONS AS PER DTC:
The permissible deductions will be the following:-

- Amount of professional tax paid;
- Transport allowance to the extent prescribed;
- Prescribed special allowance or benefit to meet expenses wholly and exclusively incurred in the performance of duties, to the extent actually incurred;
- Compensation under voluntary retirement scheme;
- Amount of gratuity received on retirement or death;
- Amount received on commutation of pension; and
- Pension received by gallantry awardees.

CONCLUSION
At this point in time, it is difficult to draw any firm conclusions about the DTC, given that it is not due to be introduced until April 2012. The aim of the DTC is to simplify tax legislation in part to attract foreign business and investment. While the Code's streamlined provisions may well achieve this, given the scope of the legislation's proposed anti-avoidance measures, companies and investors may face further uncertainty in relation to tax in the future.

ABBREVIATION

DT	:	Direct Tax
DTC	:	Direct Tax Code
CBDT	:	Central Board of Direct Taxes
IT	:	Income Tax
WT	:	Wealth Tax
RBA	:	Retirement Benefit Account
EET	:	Exempt Exempt Tax
NSC	:	National Saving Certificates
MF	:	Mutual Funds
FD	:	Fixed Deposits
NPS	:	New Pension System

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