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Concerns with Taxation proposals – Interim Budget 2019

What is the issue?

The interim Budget's tax proposals have led to certain anomalies, which needs to be corrected.

What did the government propose?

- The government recently proposed to provide full tax rebate up to Rs. 12,500 to individuals with net taxable income up to Rs. 5 lakhs in the Interim budget.
- This is under the provisions laid out in Section 87A of the Income Tax Act, 1961.
- The proposal also means that individual assesses with net taxable income above Rs. 5 lakhs will be unable to claim any rebate.
- The government reported that the proposed tax rebate would benefit three crore individual taxpayers, costing Rs. 18,500 crores to the government exchequer.
- This translates to an average relief of Rs. 6,166 per individual assesse in a year.
- However, the full benefit of the rebate, Rs. 12,500 will only accrue to individuals with net earnings at the upper limit (i.e. Rs. 5,00,000).

What are the concerns?

- There is a serious concern in the equity aspect of the proposal.
- A taxpayer, with a net taxable income slightly above Rs. 5 lakhs, will not be able to claim tax rebate and also pays a higher 20%tax according to their ceiling limit. [20% tax on net taxable income between Rs. 5 lakhs and Rs. 10 lakhs]
- Eg: A person with net taxable income between Rs. 5,00,001 and Rs. 5,16,414 will end up paying a tax of Rs. 13,000 to Rs. 16,414.
- This will result in a drop in their disposable income below Rs. 5 lakhs.
- Thus, they will not be equitably treated under the proposed changes in tax laws.

- From the data and overall distribution of gross income, around 3.6 lakh to 5.7 lakh taxpayers will be inequitably treated as per the Budget proposal.
- This unequal treatment may nudge the affected taxpayers to manipulate their income or claim inflated deductions to bring their net taxable income below Rs. 5 lakhs.
- While state-of-the-art monitoring systems of the tax authorities may successfully detect such fraudulent returns, prosecution and collection will come at a considerably high administrative cost.
- Therefore, the net benefits remain uncertain.

What should be done?

- There is one possible solution to arrive at an acceptably equitable treatment for persons with net taxable income marginally higher than Rs. 5 lakhs.
- For these taxpayers, the applicable tax amount should be the minimum ofthe calculated tax amount as per current slab rules and the amount by which their net taxable income exceeds Rs. 5 lakhs.
- Eg: If a person with net taxable income of Rs. 5,10,000 calculates her total tax as Rs. 15,080, she would actually need to pay Rs. 10,000 as a tax to bring her disposable income up to Rs. 5,00,000, ensuring parity in the tax treatment.
- Design of taxation structures is key for attaining the fiscal objectives of the government.
- An inherently inequitable tax structure, as will be the case with enactment of the proposed tax rebate, will do little to promote compliance or to expand the tax base.
- Thus, the tax rebate proposal should be aligned in such a way that it is compliant with the reforms suggested in the Direct Tax Code.

Source: Business Line

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