CHANGING BUSINESS ENVIRONMENT THRU TAXATION AND FINANCIAL REFORMS IN INDIA

Dr. Prashant Salve

What is **Tax reform?**

- **Tax reform** is the process of changing the way taxes are collected or managed by the government.
- It is usually undertaken to improve **tax** administration or to provide economic or social benefits.
- The way the government revises how tax laws are imposed.

Objectives of Tax Reforms

- To remove the present defects in existing Tax Systems
- To make it more productive (i.e., to make it more efficient from the revenue raising point of view).

(Given by Chelliah committee, appointed to examine the then tax structure of the country and suggest appropriate changes therein)

Some important recommendations made by the Chelliah Committee :

- (i) **Lowering tax rate and narrowing spread:**

In order to make the direct tax system more effective, it is necessary to reduce the tax rate so that there is less tax evasion and avoidance.

There is also the need to narrow the spread between the lowest rate and maximum marginal rate (the rate of the highest slab).

To neutralize the fall in revenue due to lowering of the rates of taxation it will be necessary to withdraw some of the tax incentives.

In other words, there is need to provide minimum tax incentives.

- **(ii) Avoiding double taxation:**

  A good tax system should not have or shall be of minimum cascading effects of taxes.

- **(iii) Reducing corporate tax rate differences between domestic and foreign companies:**
- **(iv) Rationalizing capital gains tax:**
- **(v) Rationalization of wealth tax:**
- **(vi) Tariff reduction:**
- **(vii) Rationalization of excise duty:**

History of Tax Reforms……

- **Reduction of Income Tax Rates, Introduction of various Slabs :** Present Personal Income Tax Rates reduced to 30% (MMR) as against 40% (1996), 56% (1991) from 97% (1975).

- **Introduction of Self Assessment System as against total Scrutiny Assessment or Inspector Raj.**

- Presumptive tax (lump-sum) Scheme for small traders, retailers and small business units.

- Introduction of Service Tax with 5% in 1994-95 to widen the Tax Net.

Continued…

- Reduction in Corporate Tax Rates to present 25% as against upto 39%.
- Introduction of five-year tax holiday scheme for investments in infrastructure facilities, power generation and distribution in backward states and electronics hardware and software parks.
- Reduction in Import Duties from 150% to as low as 10% on certain item.
- Introduction and extension of concept of CENVAT & MODVAT gradually.
- Electronic Filing of Returns of TDS & TCS on Tax Information Network (TIN).

Continued…

- Paperless ITR as against 24-30 pages ITR…
- Introduction Minimum Alternate (1996-97) Tax to tackle the phenomenon of zero tax companies having substantial book profits.
- Abolishment of the requirement of Tax Clearance Certificate on leaving the country.
- Establishing the Tax Information Network to modernize, simplify and rationalize tax collection, particularly TDS and TCS.

Aims of Tax Reform Measures

- Increasing resource mobilization…
- Removing anomalies and distortions in the country's tax structure through restructuring, simplification…
- Rationalization of taxes, tax systems and tax compliances…
- Targeting rising trend in tax revenue to GDP ratio…
- Easier tax filing methodology and simpler tax structures…

Recent Tax / Financial Reforms…

- Demonetization
- RERA
- Goods and Service Tax
- Benami Property Law
- Amendment in Sec. 269SS & T and introduction of Sec. 269ST in Income Tax Act 1961.
- Linking of PAN and Adhar
- Digitalization / Cashless or Less Cash Economy
- Simplified IT return filing
- *Abolition of Wealth Tax*
- *Reduction of rate of Corporate Tax*

Demonetization

PURPOSE/ NEED FOR DEMONETISATION

- High denomination notes are known to facilitate generation/ circulation of **black money**
- Total number of **bank notes in circulation rose by 40 percent** between 2011 and 2016
- **Increase in number of notes of INR 500 denomination was 76 percent and for INR 1,000 denomination was 109 percent** during this period
- Infusion of new series bank notes will be monitored and regulated by RBI
- The World Bank in **July, 2010** estimated the size of the **shadow economy for India at 20.7 percent of the GDP in 1999 and rising to 23.2 percent in 2007**
- A parallel shadow economy corrodes and eats into the vitals of the country's economy resulting in:

-**Inflation** adversely affects the poor and the middle classes
-Depriving the Government of its legitimate **revenues**
-Forged cash used to fund **terrorist activities against India**

Demonetization

PURPOSE OF DEMONETISATION

Accordingly, steps have been taken to demonetize the high denomination notes and help to:

1. **curb financing of terrorism** through the proceeds of Fake Indian Currency Notes (FICN)
2. curb the use of FICN funds for subversive activities such as **espionage, smuggling of arms, drugs and other contrabands into India,** and
3. for **eliminating Black Money** which casts a long shadow of parallel economy on our real economy

MAJOR BENEFITS

Demonetization of high denomination notes would have leap in long term benefits which could be classified as direct and indirect impact in the economy

Direct impact:

1. Fake currency - Out of circulation in one stroke
2. Hawala Sources Dried Up - Funding stops to Terrorists, Naxalites and underworld
3. Real estate prices dip to be seen in the long run
4. Reduction in inflation
5. Reduction in Fiscal Deficit
6. Reduction in lending rates
7. Increase in GDP

MAJOR BENEFITS

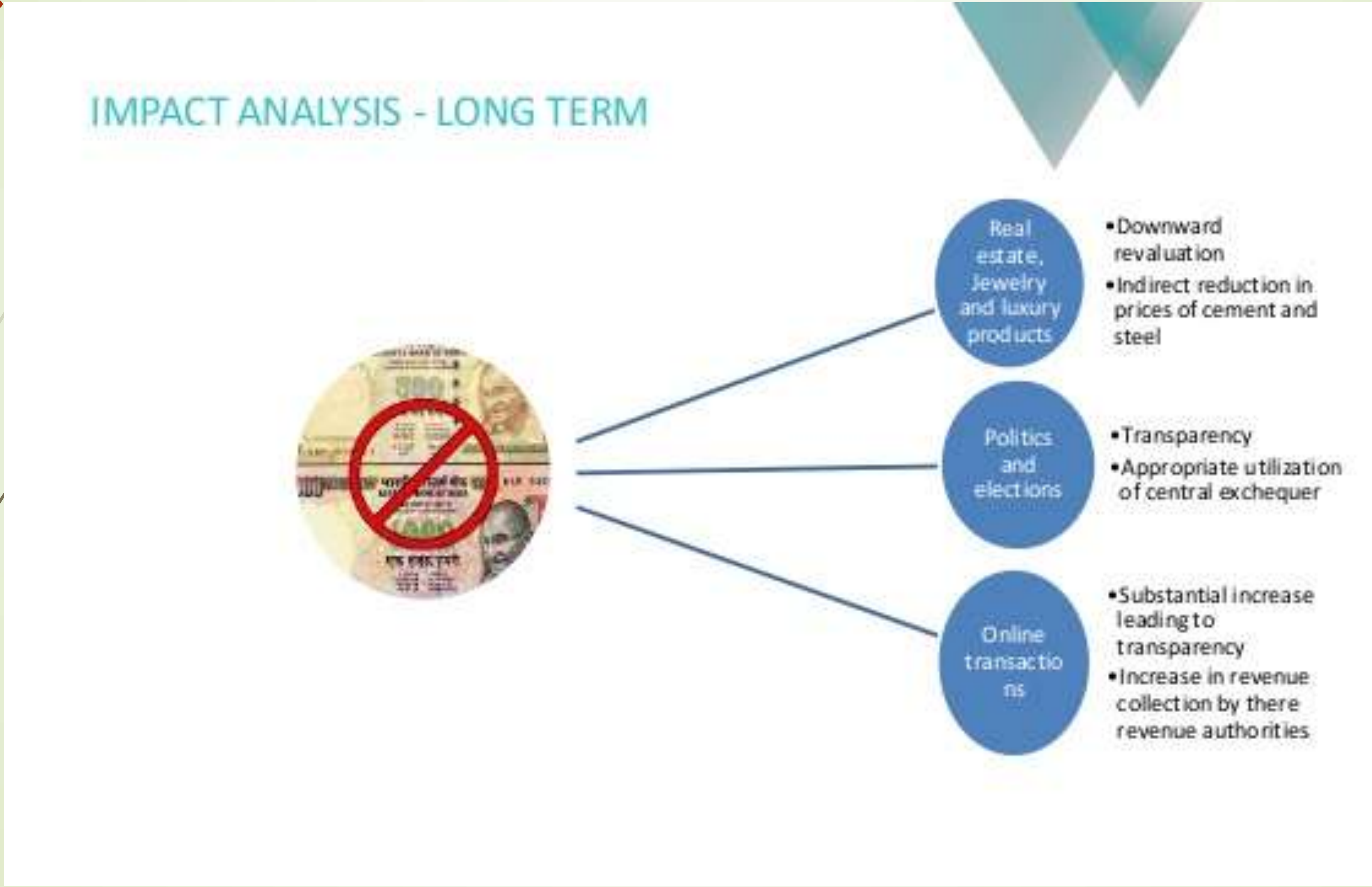
Indirect impact:

1. Kashmir moved to normalcy - Blow of insurgency, no more schools being burnt and no stone patters found
2. Use of Apps and cards - Initial step towards digitization in India with the involvement of small vendors leading to transparency in the system
3. Gold Stock - Declaration in the stock maintained by the jewelers on a day-to-day basis, which if continued would have control over generation of wealth from black money
4. Increase in revenue collection by the Government authorities
5. Simplification in tax policies and reduction in tax rates in the upcoming years

Demonetization

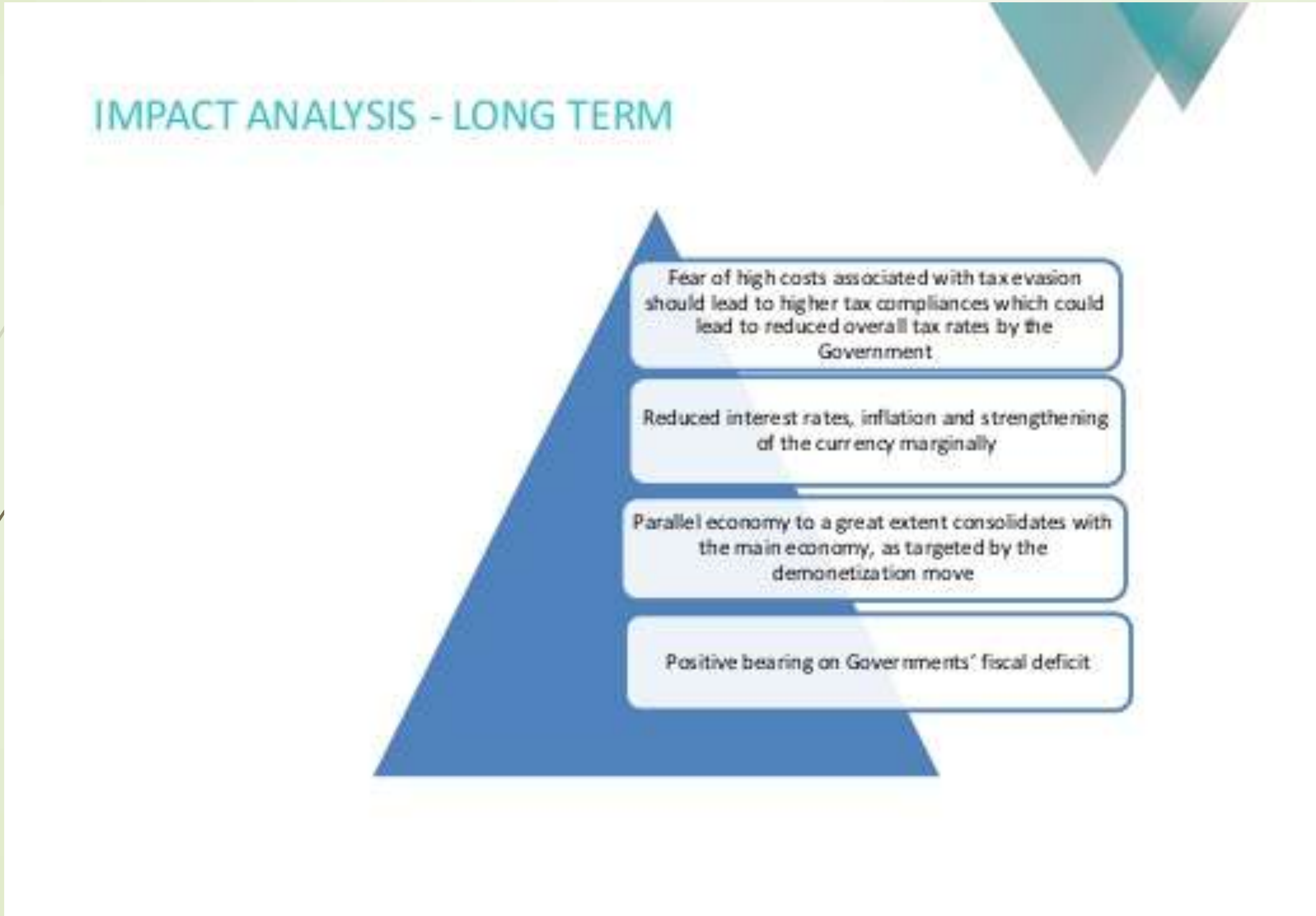
IMPACT ANALYSIS - SHORT TERM

1. **Scarcity of cash** due to demonetization
2. **Sporadic violence** wherein people attacked bank premises and ATMs with no major injuries
3. Large chunk of the **population, especially at the bottom of the pyramid and rural population highly impacted** due to poor banking facilities and extremely higher dependence on hard currency
4. Various **tribal areas living in isolation and illiteracy have been impacted adversely** in the short run
5. **Certain sectors necessitating frequent use of cash on a daily basis** including hospitals, households, roadside vendors, domestic workers, cab drivers, doctors, transporters likely to face interim disruptions
6. **Farmers may face financial difficulties** to pay daily wages to laborers in smaller denominations and manage other farming expenses
7. **Slowdown in consumer spending** due to limited availability of cash


IMPACT ANALYSIS - LONG TERM
Real estate, Jewelry and luxury products
•Downward revaluation
•Indirect reduction in prices of cement and steel
Politics and elections
•Transparency
•Appropriate utilization of central exchequer
Online transactions
•Substantial increase leading to transparency
•Increase in revenue collection by there revenue authorities


CANCELED
CANCELED

Demonetization



IMPACT ON ECONOMY - SECTOR WISE

Banking

- About **3 trillion rupees in the form of old INR 500 and INR 1000 banknotes deposited in the banking system**
- **500 billion rupees dispensed via withdrawals** from bank accounts, ATMs as well as exchanges over the bank counters
- **Spike in the usage of debit card and credit card** post demonetization was also reported

Business

- By the second week after demonetization, **sale of cigarette witnessed a fall of 30-40 percent**
- E-commerce companies saw up to a **30 percent decline in cash on delivery (COD) orders**
- E-payment options like **PayTM and PayUMoney saw a rise**
- **Real Estate** – Primary transactions may not be impacted, secondary sales may to some extent

IMPACT ON ECONOMY - SECTOR WISE

Municipal and local taxes

- Allowability of use of INR 500 and INR 1000 notes to pay municipal/ local taxes resulted in **increase in revenue collections**

Agriculture

- Adverse impact on Input-output channels in agricultural sector
- Sale, transport, marketing and distribution of ready produce to wholesale centres or mandis, adversely impacted
- Disruptions, breaks in the supply chains feedback to farmers as sales fall
- Increased wastage of perishables
- Lower revenues that show up as trade dues instead of cash in hand

Demonetization

OVERALL IMPACT

Short Run

- Whooping increase in cash deposits at banks and reduction in black money
- No affect on stock of black money which had been invested and held in other forms of assets like benami properties in land and real estate, gold, diamonds, precious gems, foreign currency, artifacts, paintings, etc
- Increase in the proportion of other assets in which black money is held, with different level of difficulties and challenges to trace the same

Long Run

- The thought remains unanswered/ un-warranted whether there is any way to prevent the generation of black money again and not re-enter the system?
- Psychological impact on the society on account of this overnight move would result in reconsidering before indulging into generation of black money
- Greater level of scrutiny at various levels and digitization coupled with sharing of information between various departments of the Government would help to keep a check on the parallel economy
- Introduction of Goods and Services Tax (GST) to play a key role to keep checks and balances

The Real Estate (Regulation & Development) Act, 2016.

- The Real Estate (Regulation and Development) Act, 2016 is an Act of the Parliament of India, which seeks to protect home-buyers as well as help boost investments in the real estate industry.
- To regulate the real estate sector, the government has come up with the idea of Real Estate Regulatory Authority (RERA) Law.
- RERA is expected to help buyers.
- RERA is supposed to protect the interest of the real estate buyer and ensure timely delivery of projects.

RERA…

Here are few ways in which buyers are likely to be benefitted by the *RERA* Act:

- Under RERA, each state will have to setup regulatory bodies as appellate tribunals to solve the disputes between buyer and builder within 120 days.
- Developer will have to put 70% of the money collected from a buyer in a separate account to meet the construction cost of the project.
- RERA will make it mandatory for all commercial and residential real estate projects where the land is over 500 sq. mt. or eight apartments will have to register with the regulator before launching a project.
- RERA also seeks to impose strict regulations on the promoter and ensure that construction is completed on time.

RERA…

- A developer's liability to repair structural defects has been increased to 5 years from the earlier 2 years.

- The buyer will pay only for the carpet area (area within walls). The builder can't charge for the super built-up area, as is the practice at present.

- Developers will be able to sell projects only after the necessary clearances. Under RERA, builders and agents will have to register themselves with the regulator and get all projects with more than eight apartments registered before launch.

- Carpet area has been clearly defined in the bill to include usable spaces like kitchen and toilets imparting clarity which was not the case earlier.

- Profile and other relevant information of the Developers will be updated on RERA Web site which will help the prospective buyers.


GST
Goods and
Services
Tax


BENAMI PROPERTY ACT

BENAMI PROPERTY (PROPERTY WHICH LACKS THE OFFICIAL OWNER'S NAME)

- Parliament had passed the Benami Transactions (Prohibition) Act, and the rules and provisions of the Benami Transactions (Prohibition) Act came into force on November 1, 2016.
- The existing Benami Transactions (Prohibition) Act, 1988, was renamed as the "Prohibition of Benami Property Transactions Act, 1988".

- Benami Property Transactions Act, 1988 has been amended by the Benami Transactions (Prohibition) Amendment Act, 2016 (BTP Amendment Act).
- The rules and all the provisions of the BTP Amendment Act shall come into force on 1st November, 2016.
- After coming into effect of the BTP Amendment Act, the existing Benami Transactions (Prohibition) Act, 1988 shall be renamed as Prohibition of Benami Property Transactions Act, 1988 (PBPT Act).

Benami (literally means 'without a name') transactions:

- Any property transaction, where the property is held by a person but the consideration for the same has been provided by another person; and the property is held for the future benefit of the person paid the consideration.
- A property transaction carried out in a fictitious name
- A transaction where owner of the property is not aware of or denies ownership
- A transaction where the person providing the consideration is not traceable or fictitious

PROHIBITION OF BENAMI PROPERTY TRANSACTIONS ACT, 1988

- The PBPT Act defines benami transactions, prohibits them and further provides that violation of the PBPT Act is punishable with imprisonment and fine.
- The PBPT Act prohibits recovery of the property held benami from benamidar by the real owner.
- Properties held benami are liable for confiscation by the Government without payment of compensation.

"Black Money is the aggregate of incomes which are taxable but not reported to authorities."

- 2015: 'The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015' has become functional now. Undeclared assets in foreign countries.
- Black money needs strict handling of laundering of untaxed money; it needs to be brought into the mainstream.
- Corruption is defined as the use of public office for private gains. Tax evasion is an illegal act of an individual or a corporate body / business. Not collecting tax is corruption.

- Demonetisation hasn't been easy on anyone but it might prove to be most damaging for small and medium enterprises, many of whom transact mostly in cash.
- Data is tough to come by but anecdotal reports and assessments made by analysts suggest that SMEs may be the hardest hit due to their reliance on cash and their limited staying power. For them, a loss of business even for a few months could prove to be debilitating.
- This, in turn, could add to the bad loan woes of Indian banks which, over the last few years, have seen non-performing assets surge. While the focus so far has been on stress emerging from large over-leveraged companies, the demonetization could lead to an incremental build up of bad loans from the SME segment.

New Section 269ST :

No person shall ***receive*** *an amount of* ***two lakh rupees*** *or more—*

(a) in aggregate from a person in a day; ***or***

(b) in respect of a single transaction; ***or***

(c) in respect of transactions relating to one event or occasion from a person,

otherwise than by an account payee cheque or an account payee bank draft or use of electronic clearing system through a bank account:

Amendment in Sec. 269SS & Sec. 269T

A Small Anti Black Money Step by Government

- The Finance Act, 2015 amended **Section 269SS** and **Section 269T** to include transactions in immovable property in order to curb black money circulation.
- Section amended by adding the sums received for **transfer of immovable property** (advance/ otherwise) whether or not ultimately the contemplated transfer takes place. Therefore, the seller of the immovable property will be liable to pay penalty on the amount accepted or taken in cash and not the buyer.
- No **repayment** of any advance received in relation to a **transfer of immovable property** would be made except by the said prescribed banking channels if aggregate is Rs. 20000/- or more. Whether the transfer takes place or not is irrelevant.

Abolition of Wealth Tax

- *Wealth Tax in India was introduced in India in the year 1957 and is levied on Individuals, HUF's and Companies if the Net Wealth of such person exceeds Rs. 30 Lakhs on the Valuation Date*

- *Mr. Arun Jaitley while announcing Budget 2015 announced that the levy of Wealth Tax has now been completely removed from Financial Year 2015-16 onwards*

- ***The loss of revenue due to the abolishment of Wealth Tax would be compensated by the levy of additional surcharge on high income earning assesses.***

- *The levy of surcharge is easy to collect & monitor and also does not result into any compliance burden on the taxpayer as well as the administration department.*

- *The information pertaining to assets which is currently required to be furnished in the Wealth Tax Return would now be required to be mentioned in the Income Tax Return.*

- ***The major reason to abolish the wealth tax was low revenue generation and high administrative burden on the government.***

- ***At the same time, it created a significant amount of compliance burden on the taxpayers, so to become taxpayer friendly, government has taken a substantial step to eliminate the unproductive tax.***

Reduction of rate of Corporate Tax

This significant move by the Government is a great economic reform that will enhance the overall tax system of the country. This will also help in enhancing the competitive edge of the nation.

- *Finance Minister Mr. Arun Jaitley extended the reduced corporate tax rate from **30% to 25%** for companies with **turnover of up to Rs 250 crore** in his Budget 2018-19 in Lok Sabha.*
- *Earlier to this year, this benefit was available only to the companies with turnover less than 50 Crores during FY 2015-16.*

- *This will benefit the entire micro and small and medium enterprises which amounts for **99% of the total companies** filing their tax returns.*

- *The estimates of **revenue foregone will be Rs 7000 crore** due to this 5% tax reduction measure, during financial year 2018-19.*

- *Out of **total 7 lakh companies filing returns, those 7000** companies which will file return with a turnover above Rs 250 crore will remain in **30% tax** slab.*

- *With this reduced corporate income tax rate for the majority of companies will enable them to offer more and more employment opportunities.*

Coming Up….
Recent Financial Reforms in India

Covering…..

- Financial Inclusion initiative
- Banking Correspondent
- NCLT
- Kotak Mahindra Bank V/s RBI
- Public Distribution System (PDS)
- Direct Benefit Transfer (DBT)
- Mahatma Gandhi National Rural Employment Guarantee Act(MGNREGA)
- Pradhan Mantri Jan Dhan Yojana, Make in India, Ayushman Bharat
- Insolvency and Bankruptcy Code

Recent Financial Frauds in India

Covering…

- *Fraud by renowned jewelers Nirav Modi*
- *IL&FS Crises*
- Kingfisher's turbulence
- Jet Airways Fiasco
- Shell Companies Network
- Rotomac Pen Scam

and many more…

Thank You