

# Direct Tax Code: Notes for IAS Exam

Direct Tax Code is a major reform in the tax system where the government aims at simplifying the tax laws and regulations into a single legislation. This article will give details about this major economic reform. The details, as a result, will be of use for candidates appearing for the IAS Exam.

## History of Implementation of Direct tax Code

The government published a discussion paper on Direct Tax Code in 2009 and issued the Direct Tax Code (DTC) bill in parliament in 2010.

Like all technical bills, this bill too was referred to the standing committee on finance headed by Mr Yashwant Sinha. The government wanted to implement DTC from 1 Apr 2012 but due to delay in the report being submitted by the standing committee, it was not possible. It is not a very controversial bill as state governments are not involved in it.

## Objectives of the Direct Tax code

The objectives of the Direct Tax Code are mentioned below:

1. To simplify and consolidate all direct tax laws of the central government
2. To make the tax system more effective and efficient.
3. To bring the consolidated law relating to direct taxes, that is, income-tax, dividend
4. distribution tax, fringe benefits tax and wealth-tax
5. To bring horizontal equity among different classes of taxpayers in line with best international practices.
6. To improve compliance further, tax laws need to be simple, stable and robust.
7. To phase out the multiplicity of tax exemptions and deductions in order to widen and deepen the tax base.

## What is simplification and consolidation of Direct tax Laws?

**Simplification of direct tax laws can be stated as follows:**

- Tax laws would be re-written in simple language
- Exemptions and reductions would be reduced
- Cross-references will be reduced
- Explicit Language will be used.

**Consolidation of tax laws can be stated as follows:**

- All tax laws dealing with direct taxes would be merged.
- E.g. Income Tax Act, 1961; Wealth Tax Act, 1957; Gift Tax Act, 1958.

## **Direct Tax Code (DTC) Proposals**

- Increase in Income tax slabs. (Government adopted the proposed tax slabs in the financial year 2012 – 2013)
- Corporate Income Tax or Corporate Tax – For both domestic and foreign firms, the tax rate should be 30% and no surcharge will be applicable. Currently, there is a 5% surcharge that is applicable for domestic firms and for foreign firms, tax is 40% along with 2% surcharge is also applicable.
- Minimum Alternate Tax rate should be 20%. Currently, the tax rate of MAT is 18.5%.
- Savings Scheme should be under EET. Presently these schemes are under EEE.
- Few schemes like PF, Gratuity, pension funds etc would still come under EEE.

## **GAAR – General Anti Avoidance Rule**

GAAR is a provision in the direct tax system which aims at providing discretionary power to tax officials to deny and tax benefit to any firm. However, Tax officials can violate certain provisions of the Income Tax Act and Double Taxation Avoidance Act

The main advantage of this rule is that there will be a major reduction in tax avoidance in order to check the misuse of DTAA. This General Anti Avoidance Rule will impose restrictions on round-tripping.

However, there are certain disadvantages of GAAR which are stated below:

- It provides discretionary powers to tax officials
- Corruption may increase
- Uncertainty will increase
- Creditworthiness will decrease

## **Guidelines issued by the government in the implementation of GAAR**

The major guidelines issued in the implementation of GAAR are:

- Approving panel should be established having 3 high ranking Income Tax officials
- GAAR will be invoked only for large transactions.

Parthasarathi Shome committee recommendations:

- GAAR should be postponed for 3 years i.e. 1st April 2016.
- Whether GAAR has to be invoked or not should be decided by the approving committee.
- Threshold limit to be set as 3 crores.

- Capital gains tax should be abolished and the advanced ruling should be allowed.
- Tax residency certificates by governments of other countries should be accepted
- The prime objective of GAAR should be to check misuse of tax and it should be invoked only in contravention cases.
- If Specific anti-avoidance rules are present then GAAR should not be invoked.
- The Shome panel also recommended that retrospective amendment should be made only in rarest of rare cases.