

DIRECT TAXES CODE BILL – HIGHLIGHTS

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The Honourable Finance Minister released the draft Direct Taxes Code and the Discussion paper on 12th August 2009. An attempt has been made to simplify the language to enable better comprehension and to remove ambiguity to foster voluntary compliance.

1. PRELIMINARY

- This Code shall be called the Direct Taxes Code, 2009
- It extends to the whole of India.
- It shall come into force on the 1st day of April, 2011; i.e. Financial Year 2011-12.

2. BASIS OF CHARGE

- **RESIDENTIAL STATUS:** Only status of “Non Resident” and “Resident of India” exists. The other status of “resident but not ordinarily resident” has been removed.
- **TOTAL INCOME:** Total Income to include income of any other person. Total Income to include income of spouse, minor child etc. Also, the total income for a financial year of any person shall not include any of the income.

3. COMPUTATION OF TOTAL INCOME:

- **CLASSIFICATION OF SOURCES OF INCOME:** For the purpose of computation of total income of any person for any financial year, income from all sources shall be classified into :

a) **Income from Special sources** are given no deduction and what is earned is taxed directly.

The steps for computation of income from special sources are as under:

STEP 1: Compute the income in respect of each of these special sources in accordance with the provisions of the Fourth Schedule. The income so computed with respect to each of such special sources shall be called ‘current income from the special source’.

STEP 2: Aggregate the ‘current income from the special source’ with the unabsorbed loss from that special source at the end of the immediate preceding the financial year, if any. The result of such aggregation shall be the ‘gross income from the special source’. If the result of aggregation is a loss, the ‘gross total income from the special source’ shall be ‘nil’ and the loss will be treated as the ‘unabsorbed current loss from the special source’, at the end of the financial year. The ‘gross total income

from the special source' shall be computed with respect to each of the special sources.

STEP 3: The gross total income from all such special sources and the result, of this addition shall be the 'total income from special sources'.

b) Income from Ordinary sources are divided into further categories, namely:

1. Income from employment (Presently called Salaries)
2. Income from House Property
3. Income from Business
4. Capital gains
5. Income from Residuary Sources (Presently called other sources)

The steps for computation of income from ordinary sources are as under:

STEP 1: Compute the income in respect of each of these sources. This could either be income or loss (negative income). For example, if a person carries on several businesses, the income from each and every such business will have to be separately computed.

STEP 2: Aggregate the income from all the sources falling within a head to arrive at a figure of income assessable under that particular head. The result of such computation may be a profit or loss under that head.

The aforesaid two steps will be followed to compute the income under each head.

STEP 3: Aggregate the income under all the heads to arrive at the 'current income from ordinary sources'.

STEP 4: Aggregate the current income with the unabsorbed loss at the end of the immediate preceding financial year, if any, to arrive at the 'gross total income from ordinary sources'. If the result of aggregation is a loss, the 'gross total income from ordinary sources' shall be 'nil' and the loss will be treated as the 'unabsorbed current loss from ordinary sources' at the end of the financial year.

STEP 5: 'Gross total income from ordinary sources', so arrived, will be further reduced by incentives in accordance with sub-chapter I of Chapter III. The resultant amount will be 'total income from ordinary sources.'

- **AMOUNT NOT DEDUCTIBLE WHERE TAX IS NOT DEDUCTED AT SOURCE:**
Any amount on which tax is deductible at source under Chapter XI during the financial year shall not be allowed as a deduction in computing the total income if:
 - a) the tax has not been deducted during the financial year; or
 - b) the tax, after such deduction, has not been paid during the financial year, or in the subsequent year, before the expiry of the time prescribed under sub section (1) of Section 198.

However, the provision of sub section (1) shall not apply, if the tax has been deducted during the last quarter of the financial year and the tax is paid before the due date of filing the return of tax bases.

4. **INCOME FROM EMPLOYMENT:**

- Income from employment will be the gross salary on due or receipt basis, whichever is earlier including value of perquisites and profits in lieu of salary as reduced by the aggregate amount of the following permissible deduction.
 - a) Professional Tax paid;
 - b) Transport Allowance to the extent prescribed;
 - c) Prescribed Special Allowance or benefit to meet expenses wholly and exclusively incurred in the performance of duties, to the extent actually incurred;
 - d) Compensation under Voluntary Retirement Scheme
 - e) Amount of gratuity received on retirement or death;
 - f) Amount received on commutation of Pension; and
 - g) Pension received by gallantry awardees.
- The value of rent free accommodation will be determined for all employees in the same manner as is presently determined in the case of employees in the private sector.
- All perquisites to be included in Salary Income.
- There is no deduction on HRA and medical reimbursement.

5. **INCOME FROM HOUSE PROPERTY:**

- Income from house property, which is not occupied for the purpose of any business or profession by its owner, will be taxed under the head “Income from house property”.
- The income from property shall include income from the letting of any buildings along with any machinery, plant, furniture or any other facility if the letting of such building is inseparable from the letting of the machinery, plant, furniture or facility.
- No deduction in respect of municipal taxes and interest for self occupied house whose gross rent is taken as Nil.
- Only Let out properties are considered and the Gross rent and specified deductions are allowed. The Income from house property shall be the gross rent less specified deductions.
- The following deduction will be admissible against the gross rent:-
 - a) Amount of taxes levied by a local authority and tax on services, if actually paid.
 - b) Twenty per cent of the gross rent towards repairs and maintenance
 - c) Amount of any interest payable on capital borrowed for the purpose of acquiring, constructing, repairing, renewing or re-constructing the property.

6. **INCOME FROM BUSINESS:**

- Every business will constitute a separate source and, therefore, income will be computed separately for each business.
- A business will be treated as distinct and separate from another business if there is no interlacing or independence or unity embracing the two businesses.
- The computation of income from business under the Code will be based on the income-expenses model where the taxable income under this head will be equal to gross income minus allowance deductions.
- Indefinite carry forward of business losses to be allowed.

7. **CAPITAL GAINS**

- Income from transactions in all investment assets (i.e. any capital asset other than business capital asset) will be computed under the head "Capital Gains".
- The present distinction between short term investment asset and long term investment asset on the basis of the length of holding of the asset will be eliminated.
- The Securities Transaction Tax will be abolished. Therefore, all capital gains (loss) arising from the transfer of equity shares in a company or units of an equity oriented fund will form part of the computation process.

8. **INCOME FROM RESIDUARY SOURCES**

- The gross residuary income will comprise of any income which does not from part of any other head of income.
- Any amount exceeding Rs.20,000 taken or accepted or repaid as loan or deposit otherwise than by account payee cheque or draft shall be deemed to be income from residuary sources and taxed accordingly.
- 'Any sum received under Life Insurance Policy, including any bonus, shall be exempt from Income Tax, provided it is a pure life insurance policy (i.e. the premium payable for any of the years during the terms of the policy does not exceed 5 percent of the capital sum assured). Consequently, in all other cases, the sum received under the policy, including any bonus, will be taxed as income from residuary sources.

9. **EET METHOD OF TAXING SAVINGS**

- The Code proposes to introduce the 'Exempt-Exempt-Taxation' method of taxation of savings.
- Only new contributions on or after the commencement of this Code will be subject to the EET method of taxation.
- An individual or HUF will also be allowed deduction for amount paid towards tuition fees for children. The aggregate amount of deduction for payment into the account maintained with any permitted savings intermediary and for tuition fees shall not exceed Rs. 3 Lakhs.

10. TAX INCENTIVES:

- Major Deductions applicable under the Tax Incentives for an individual are:
 - a) Investments through PFRDA approved agencies
 - b) Payment of tuition fees
 - c) Medical treatment
 - d) Health insurance
 - e) Donations
 - f) Interest on loan taken for higher education
 - g) Maintenance of a disabled dependant
 - h) Interest income on Government Bonds.
- Earlier terms Deductions under Chapter VI A will be treated as Tax incentives.
- Medical treatment, higher education loan interest, donation and rent paid by self-employed individual are deductible.
- New provision comes for Handicapped individuals to get deductions upto Rs. 75,000.

11. TAXATION OF COMPANIES:

- Dividend Distribution Tax(DDT) to be retained. Dividends which suffered DDT to be tax-free in shareholder's hands.
- The Code provides for Minimum Alternate Tax calculated with reference to the "value of the gross assets". The shift in the MAT base from book profits to gross assets will encourage optimal utilization of the assets and thereby increase efficiency.
- The rate of MAT will be 0.25 percent of the value of gross assets in the case of banking companies and 2 percent of the value of gross assets in the case of all other companies. Under the code, MAT will be a final tax. Hence, it will not be allowed to be carried forward for claiming tax credit in subsequent years.

12. WEALTH TAX:

The Code proposes to tax net wealth in the following manner:

- Wealth-tax will be payable by an individual, HUF and private discretionary trusts.
- Wealth-tax will be levied on net wealth on the valuation date i.e. the last day of the financial year.
- Net Wealth will be defined as assets chargeable to wealth-tax as reduced by the debt owed in respect of such assets.
- The net wealth of an individual or HUF in excess of Rs. 50 Crores will be chargeable to wealth tax at the rate of 0.25 per cent.
- The threshold limit of Rs. 50 Crores will not apply to a private discretionary trust.

13. NEW TAX RATES FOR INDIVIDUALS:

- In the case of every individual, other than women and senior citizen:

Slab	Income Between	Tax rate
1	0 - 1.60 Lakhs	0%
2	1.60 Lakhs to 10 Lakhs	10%
3	10 Lakhs to 25 Lakhs	20%
4	Above 25 Lakhs	30%

- In the case of woman below the age of sixty five years at any time during the financial year:

Slab	Income Between	Tax rate
1	0 - 1.90 Lakhs	0%
2	1.90 Lakhs to 10 Lakhs	10%
3	10 Lakhs to 25 Lakhs	20%
4	Above 25 Lakhs	30%

- In the case of senior citizens:

Slab	Income Between	Tax rate
1	0 - 2.40 Lakhs	0%
2	2.40 Lakhs to 10 Lakhs	10%
3	10 Lakhs to 25 Lakhs	20%
4	Above 25 Lakhs	30%

14. DUE DATE FOR FILING RETURNS OF TAX BASES:

Sl. No	Type	Date	First filing (under Direct Taxes Code)
1	Non-Business / Non-Corporate	30th June	30/06/2012
2	Others	31st August	31/08/2012

15. OTHERS:

- The terms 'previous year' and 'assessment year' has been replaced with 'financial year' to eliminate confusion.
- Income for the purposes of this Code will, in general, include all accruals and receipts of revenue and capital nature unless otherwise specified.
- Taxation for non – profit organizations rationalized.
- Mutual Funds, Venture capital funds, Life Insurance Companies to be treated as pass – thru entities.
- Earlier Income Tax Act and Wealth tax Act (Covering Income Tax, TDS, DDT, FBT and Wealth taxes) are abolished and single code of Tax, DTC in place.
- Only status of “Non Resident” and “Resident of India” exists. The other status of “resident but not ordinarily resident” has been removed.
- Earlier the terminology of assessee was meant for the person who is paying tax and/or, who is liable for proceeding under the Act. Now it has been added with 2 more definitions namely a person, whom the amount is refundable, and/or, who voluntarily files tax return irrespective of tax liability. This helps any person to file his returns and maintain the record of tax return filing.
- No changes in the system of Advance Tax, Self Assessment Tax and also TDS. Amendment of TDS goes in line with earlier Notification 31/2009 which speaks of Form 17/UTN/etc. In TDS, a new return, if found required, will be introduced for Non TDS payments.
- Government assessee is covered in Direct Tax Code. Even though they are not liable for Income Tax / Wealth Tax, Government Assesseees are required to Comply with provision of TDS and TCS. (Current act was not covered with Government Assesseees).
- General anti – avoidance rule introduced to combat tax avoidance.
- Amalgamation and demerger provisions rationalized to allow for tax neutral business reorganization.

Conclusion

To conclude, this code is broadly welcomed by the industry and the trade. However, there are reactions on some points which are shown below:

- Tax on interest on overseas borrowing is a negative factor and it may discourage leveraging and reduce investment
- The proposal to apply MAT on Gross assets instead of book profit has come under heavy criticism from industry because it is not a tax on income, which direct tax should ideally be, but a tax on capital or assets. Also, because it is value of gross assets, even loss making companies have to pay MAT.
- MAT at 2% of gross assets is a very high rate
- The issue of MAT on financial companies has also come under criticism because while MAT in the code for the Banking sector is set at 0.25%, it is at 2% for the NBFCs (Non Banking Finance Companies)

Comments / feedback on the Direct Tax may be sent to FKCCI at dsm@fkcci.in

