Chapter 1

RECENT CHANGES IN INCOME TAX PROVISIONS - AN OVERVIEW
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In the traditional economy, the Role of Government was limited to the maintenance of law and order and the government interference in the economy was considered unnecessary. But with the passage of time, the interference of the Government in economy has become inevitable because in modern times apart from its traditional functions of defence and maintenance of law & order, a modern government undertakes welfare and developmental activities and makes provision for public goods to satisfy collective needs of the people. It has also to pay for its own administration and has the responsibility of protecting the citizens, promotion of their economic and social welfare etc. So, it needs financial resources for these purposes and taxation is one method of transferring of money from private to public hands. The methods usually open to any modern government for increasing its revenue are tax and non tax revenues (imposing taxes on income, properties, charging for goods and services it provides, borrowing loans, printing currency, coinage and mint, interest receipts, dividends etc). So, while the government often uses a judicious mix of all the alternatives of raising resources, taxation is the most important source of government revenue. Philosophy behind such taxation is that the society should itself pay for its development. According to Kalidas the greatest Sanskrit poet of ancient Indian “just as the sun extracts water from the reservoirs and give it back in the form of showers, so does the ruler extract tax from his subjects and give it back to them in the form of prosperity”.

Tax systems the world over have undergone significant changes during the last twenty years, as many countries across the ideological spectrum
and with varying levels of development have undertaken reforms. The wave of tax reforms that began in the mid-1980s and accelerated in the 1990s was motivated by a number of factors but fiscal crisis has been proven to be mother of tax reform. In many developing countries, tax policy was used as the principal instrument to correct the fiscal imbalances. In others, the transition from a planned economy to a market economy necessitated wide ranging tax reforms. Besides efficiency considerations, these tax reforms had to address the issues of replacing public enterprise profits with taxes as a principal source of revenue and of aligning tax policy to change in the development strategy. Another motivation was the internationalisation of economic activities arising from increasing globalisation. On the one hand, globalisation entailed significant reduction in tariffs, and replacements had to be found for this important and relatively easily administered revenue source. On the other, globalisation emphasised the need to minimise both inefficiency and compliance costs of the tax system. The supply-side tax reforms of the Thatcher–Reagan era also had their impact on the tax reforms in developing countries.

The reforms in Indian tax system in some respects are unique and reforms are broadly in conformity with international trends of broadening of base, reducing the rates, reducing the rate differentiation and keeping the system simple and advice proffered by the expert groups and Indian tax reforms are in tune with international best practices.

**Taxation in India**

The present Indian fiscal system is centuries old and this was introduced by the British in the year 1860 based on the English system of taxation and there after various additions and amendments were incorporated to
suit their requirements from time to time. After the achievement of Independence and the National Government’s commitment for rapid and balanced economic development of the country, provided income tax an important place in the public finance of the central Government and appointed taxation enquiry commission headed by John Mahtai to make an in-depth study of the structure and possibilities of using taxation as an instrument of Economic policy. The Income tax Act was there after referred to the law commission and recommended a comprehensive law on income tax. Then Direct Tax Administration Enquiry Committee (Tyagi committee) submitted a detailed report in 1959 resulting in the Income Tax Act, 1961 which holds the field even today though substantially changed by frequent amendments from 1961 till now.

The direct taxation of the income of individuals, companies and other entities is governed by the Income Tax Act, 1961. The Act specifies the entities to be taxed, the kinds of incomes subject to tax (or exempt from tax), and the tax rates to be imposed on them. It lays out a system by which taxes are to be assessed and collected and specifies a procedure by which disputes with tax authorities are to be addressed. Changes to income and wealth tax (including tax rates) are introduced in Parliament in the form of an annual Finance Bill which amends the Income Tax Act and the Wealth Tax Act, 1957.

The income tax Act determines which person are liable to pay tax and in respect of which income. The various sections lay down the law of income tax and schedules elucidate certain procedures and give certain lists which are referred to, in the sections. However, the Act does not prescribe the rates of income tax. These rates are prescribed every year by the finance Acts (popularly known as “The Budget”). Income tax Act 1961, consists of 298 sections and 14 schedules with numerous sub-
sections. It is almost 5 decades old and nearly 5,000 amendments were made in the existing income tax Act, 1961 as a result, it became more complicated and it is beyond the understanding of the most of the taxpayers, encourage for tax evasion and tax avoidance and also the incidence of taxation in urban areas is much higher than in the rural areas because of the main occupation of the rural areas is agriculture and income from agriculture has been kept outside the preview of income tax.

**Constitutional provisions pertaining to taxes in India**

The Apex body of the income department is the Central Board of Direct Taxes (CBDT) manned by the officers of the Indian revenue Service and it performs various statutory functions. Income Tax Act, 1961 also empowers the CBDT to formulate rules for implementing the provisions of the Act. Article 265 of the constitution specifically states that no taxes shall be levied and collected except by the authority of law. Entries 82 to 92B of the list I, list II in the seventh schedule refer to the taxation powers of the Union Government and State Governments respectively. The constitution does not provide for any taxation powers to the local Governments. However, the implication of Article 276 is that the taxes on professions prescribes trades, employment are for the benefit of the state.

An Article 270 prescribes taxes on income other than agricultural income (Entry 82 of union list) is to be shared between Central and State governments as per the basis provided by the Finance Commission. The constitution of India vests the parliament with plenary legislative powers to impose taxes on matters specifically enumerated in the union list and all the powers of making any law imposing tax not mentioned in concurrent list as provided by Article 248(2).
Sharing of taxes

Although the taxation powers allocated to the Union and the States are mutually exclusive, all the taxes and duties levied by the Union are not meant entirely for the purpose of the Union. Earlier, under Article 270, taxes on income other than agricultural income (entry 82 of the Union List) were levied and collected by the union and distributed between the Union and the States on the basis provided by the Finance Commission. The constitution (Eightieth Amendment) Act, 2000 substituted a new article for Article 270 under which states are now given a percentage share of all central taxes and duties. However, the surcharge levied for the purpose of Union under article 271 is excluded from the divisible pool.

Tax structure

Tax structure refers to the various taxes that constitute the tax system of a country, broadly comprising direct and indirect taxes. India has a tax structure with three tier federal structure (the Union Government, State Governments and the urban/rural local bodies). The Indian tax system comprises direct taxes like personal income tax, corporation tax, wealth tax, gift tax, (till1998), land revenue, agricultural income tax, expenditure tax (on the expenditure incurred in hotels and restaurants) and indirect taxes like customs, Union excise duties, state excise duties, stamp and registration fees, sales tax, tax on vehicles, entertainment tax, tax on goods and passengers, tax on electricity, VAT etc. Excepting land revenue and agricultural income tax, all the other direct taxes are levied and collected by the Central Government and except the customs and union excise duties and additional duties of excise, all other indirect taxes are levied and collected by the State Governments according to the provisions made in the Indian constitution regarding the sharing of tax
powers between the centre and the states. Indirect taxes occupied the dominant position in Indian tax system till the tax reforms were initiated but the trend towards increase in the share of direct taxes and decrease in the share of indirect taxes can be seen after 1991 tax reforms.

A comparison between the Indian tax structure and its counterparts prevailing in other developing countries relatively shows a somewhat outdated picture. The total Indian fiscal pressure is just slightly lower than the figure prevailing in those countries where per capita income is near to the Indian value. However, Indian direct taxes appear comparatively very low has been increasing after tax reforms in 1991, while indirect ones stay quite high has declined and share of import duties is relatively low.

**Recent reforms/Changes in the Indian tax system**

There have been major changes in tax systems of countries with wide variety of economic systems and levels of development during the last two decades. The motivation for these reforms has varied from one country to another and thrust of reforms has deferred from time to time depending on the development strategy and philosophy of the times. In many developing countries, the immediate reason for tax reforms has been the need to enhance revenues to meet impending fiscal crisis. One of the most important reasons for recent tax reforms in many developing and transitional economics has been to evolve a tax system to meet the requirements of international competition.

The recent tax reforms are, in fact, a continuation of the reforms initiated in 1991. In this sense, tax reform in India has been gradual and although not always consistent from year to year, the overall direction has been
broaden the tax bases, reduce the rates, reduce rate differentiation and make the tax system simple and transparent. During the period under study, the following are the some of the major changes brought in Indian tax system through budget proposals.

1. Restructuring individual income tax rates

The individual income tax rate structure in India is mainly based on ability to pay principle, which gets reflected in the level of income. The exemption limit and income brackets in which income is divided for tax purposes and the rates at which income tax is levied determine the incidence of tax on a person.

Individual income tax rates in India were at their peak for the period from 1971-72 to 1973-74, with the exemption limit at Rs. 5,000, the minimum marginal rates of tax at 10 per cent, and the maximum marginal rates of tax rising to 85 per cent spread over eleven tax slabs. The design of the tax rate schedule was neither economically efficient nor equitable. Such high rates not only made tax administration very difficult, but also led to a state, where income tax evasion became widely accepted as standard behavior. Since those days, there was a steady increase in exemption limit, decrease in the maximum marginal rate of tax, and reduction in the number of tax slabs. As a result, the design of tax rate schedule was made more efficient, the number of tax rate slabs was also reduced substantially.

Tax Reforms Committee, under the chairmanship of Raja J. Chelliah, in its interim report observed that the best results in terms of compliance (and, therefore, revenue efficiency) and equity can be obtained through a system incorporating moderate rates on a broad base. It is well recognised
that the rates of tax affect the economic behavior of taxpayers i.e., choice between work and leisure, the choice between consumption and savings, and also the compliance behavior of taxpayers. The design of individual income tax rate schedule therefore must be equitable and efficient, which are potentially conflicting objectives. A high progressive rate schedule, while meeting the ends of vertical equity, causes higher distortions in the economic behavior of taxpayers and therefore promotes inefficiency. Further, high rates of tax induce tax evasion, thereby undermining the effective impact on equity, apart from raising the exemption limit; rate structure has been altered in accordance with the new policy of taxation with stress on moderate rates.

After the recommendations made by Tax Reforms Committee in 1991, tax rate structure has been substantially lowered and with effect from financial year 1997-98, maximum marginal rate of tax have been reduced to 30 per cent. The exemption limit for the assessment year 1999-2000 was Rs. 50,000 and there was no change in the tax rate till the assessment year 2003-2004. Also with effect from financial year 2004-05, exemption limit was raised to Rs. 1,00,000 for individuals. With effect from 2007-2008 the exemption limit was raised to Rs. 1,10,000 (other than women assesses and senior citizens) Rs. 1,35,000 for women assesees and Rs. 1,85,000 for senior citizens. For the financial year 2008-09, exemption limit is Rs. 1,50,000 for individuals, Rs. 1,80,000 for women assesses and Rs. 2,25,000 for senior citizens. Again, the exemption limit was raised to Rs.1,60,000 for all categories of individual tax payers in 2009-2010 but in case of senior citizens, it was raised by Rs. 15,000 from Rs. 2.25 lakh to Rs. 2.40 lakh; by Rs.10,000 from Rs.1.80 lakh to Rs. 1.90 Lakh for women taxpayers.
The given changes in respect of exemption limit and rate structure served the objective of ushering in an era of moderate tax rates with the hope that this will contribute to an improvement in tax compliance.

2. Corporate tax rates

The taxability of a company’s income depends on its domicile. Indian companies are taxable in India on their worldwide income. Foreign companies are taxable on income that arise out of their Indian operations or in certain cases income that is deemed to arise in India, royalty, interest, gains from sale of capital assets located in India. In most of the countries with income taxation, it is a practice to tax the profits of corporate entities. The classical system of taxing corporate income was adopted in India since 1959-60. The classical system treated the company and the shareholders as separate legal entities. The domestic company tax rate has been reduced from 55 percent in 1984-85 to 45 percent in 1994-95.

The Chellaiah committee recommended systematic reduction of the corporate tax. Till the last decade, corporate income tax rates in India were very high vis-à-vis other countries. Efforts have been made to reduce the tax rates. Even then, there has been erosion in the tax base but the rates of corporate tax are gradually have been reduced. In case of corporate taxes too the tax structure has remained stable since 1997-98 when the rate was brought down to 35 percent and it has been reduced to 30 percent in 2006-2007 and there was no change in corporate tax rates during the last four years.

The corporate tax rate was 38.50 percent, 39.55 percent, 35.70 percent, 36.75 percent, 35.875 percent, 36.60 percent, 33.66 percent, 33.66 percent, 33.99 percent and 33.00 percent with surcharge for domestic
companies in 1999-00, 2000-01, 2001-2002, 2002-2003, 2003-2004, 2004-2005, 2005-06, 2006-07, 2007-08, 2008-09 and 2009-10 respectively including surcharge and cess. Whereas for foreign company’s dividends are charged at 20 Percent, interest income at 20 Percent, technical services at 30 Percent and other income at 55 Percent. The corporate taxes were remained unchanged in most of the years under the study except with change in surcharge. The effective tax rate of companies in 1999-00 was 21.7 percent as against the statutory rate of 38.5 percent. Similarly, the effective tax rate of companies in 2000-2001 was 21.9 percent as against the statutory rate of 39.55 percent. This is despite the provisions of the minimum alternative tax (MAT), various concessions and exemptions under various sections of the income tax Act.

Other changes in the corporate tax structure in recent years include: Reduction of the tax rate from 30 to 20 percent on royalty and technical services fees payable to foreign companies; modification of the minimum alternate tax (MAT) on companies; abolition of tax on dividends in the hands of the shareholders; and imposition of a tax on distributed profits at the moderate rate of 10 percent. This is to induce companies to retain the bulk of their profits and plough them into fresh investments. The corporation tax yielded revenue of Rs. 40 crore in 1950-51, which was about 30 percent of personal income tax. It rose to Rs. 1,310 crore is 1980-81 and it was less than the personal income tax revenue. Under the impact of economic planning and rapid industrialisation, the yield from corporate tax has been rising steadily. The corporation tax is expected to yield Rs. 2,56,725 crore in 2009-2010 reflecting the growing industrialisation in the country. At present the corporation tax is the single largest revenue-yielding tax in the country.
3. Surcharge on various direct taxes

It is charge or tax levied on the tax payers whose income exceeds certain limit. The surcharge was introduced in the Indian tax system to raise additional revenue. The percentage of surcharge was 12 Percent in 2001-2002 if the total taxable income exceeds Rs. 60,000 and it was 17 Percent if the taxable income was more than Rs.1,50,000 but in the year 2002-03 it was reduced to only 2 Percent, if the taxable income was more than Rs. 60,000 and it was raised to 5 Percent in 2003-2004 if the taxable income was more than Rs. 1,60,000. But in 2004-05 and 2005-2006 it was raised to 10.5 percent if the taxable is more than Rs. 8.5 lakh. Again in 2006-2007, 2007-2008 and 2008-2009 it was remained unchanged up to Rs. 10 lakh. But with effect from 2009-2010 assessment year it has been abolished.

4. Fringe benefit tax

Introduction of fringe benefit tax (FBT) is a tax chargeable under section 115W. Apart from the income tax payable, an additional tax shall be charged for every assessment year commencing on or after 1st day of April 2006 in respect of the fringe benefits provided or deemed to have been provided by an employer to his employees at 30 percent on the value of such fringe benefits. Fringe benefit tax was introduced as a revenue rising measure. This can be justified on the principles of horizontal equity and vertical equity.

Fringe benefit means (a) any privilege, service, facility or amenity directly or indirectly provided by an employer to his employees. (b) Any reimbursement made by employer to his employee. (c) Any free concessional ticket provided by the employer to his employee and/or his
family for private journeys. (d) any contribution made by employer to an approved superannuation fund.

Fringe benefit shall be deemed to have been provided if the employer made payments for following purposes (1) Entertainment (2) Festival Celebrations (3) Gifts (4) Use of club facilities (5) Provision of hospitality by employer to any person (6) Maintenance of accommodation like guest houses (7) Conference (8) Employees welfare (9) use of health club, sports and similar facilities (10) sales promotion and publicity (11) Conveyance, tour and travel (12) Hotel boarding and lodging (13) Repair, running and maintenance of motor cars (14) Repair running and maintenance of air craft (15) Consumption of fuel other than industrial fuel (16) use of telephone (17) scholarship to children of the employees.

FBT for all employers, in general six months of sales promotion and advertising expenses will be excluded while estimating the fringe benefits to be taxed. The base value on all categories of defined fringe benefit expenditure barring four shall be 20 Percent for levy of tax. Taxable value of benefit for tour and travel reduced from 20 Percent to 5 Percent. Rationalisation of FBT for expenditure of traveling, hotel lodging, boarding and hospitality. Certain expenditure exempted from the purview of FBT. Beneficial rate of valuation of the fringe benefit at 5 Percent for traveling expenditure is now extended to all industries. This was earlier applicable only to pharma, computer software and construction sectors. Further expenditure on hotel lodging, boarding and hospitality incurred by shipping and airline companies will also now be valued at 5 Percent. Free samples of medicine and medical equipment to doctors and payment to brand ambassadors will not be subject to FBT. Many companies
provide fringe benefits to employees through employees stock option plan (ESOP). Hence ESOP is brought under FBT.

Without prejudice to the provisions contained in section 139, every employer who during a previous year has paid or made a provision for payment of fringe benefits to his employees, shall on or before the due date furnish or cause to be furnished a return of Fringe benefits to the assessing officer in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed, in respect of the previous year. If any person being employer fails to make the return, the assessing officer make assessment of the fringe benefits to the best of his judgment and determine the sum payable by the assessee on the basis of such assessment. The tax on fringe benefits shall be payable in advance during the financial year otherwise interest will be charged.

5. Minimum Alternate tax (MAT)

Normally, a company is liable to pay tax on the income computed in accordance with the provisions of the income tax act, but the profit and loss account of the company is prepared as per the provisions of the companies Act. There were large number of companies who had book profits as per the profit and loss account but were not paying any tax because income computed as per the provisions of the income tax Act was either nil or negative or insignificant. In such case, although the companies were showing book profits and declaring dividends to the shareholders, they were not paying any income tax. These companies are known as zero tax companies. In order to bring such companies under the
income tax Act net, section 115JA was introduced w.e.f assessment year 1997-98 at 30 Percent of its book profit.

The provisions of this section remained in force for four years, before being withdrawn by the Finance Act 2000 with effect from April 01, 2001 introduced section 115JB. Where under tax at the rate of 7.5 percent on the book profit being levied. This was modified by Finance Act 2002, at 7.5 percent plus surcharge on such book profits and remained unchanged till 2005-2006. With effect from 2006-2007, marginal revision in certain tax rates in the quest for equity. MAT rate increased from 7.5 percent of book profits to 10 percent which is only one-third of the normal rate; long term capital gains arising out of securities included in calculating profits; period to take credit for MAT increased from five to seven years.

With effect from 2007-2008, MAT was extended to all the incomes which were claimed as deduction under section 10A and 10B and deduction under section 36(i)(vii) was restricted to 20 percent of profits each year. But in 2008-2009 there was no change in the MAT, where as in 2009-2010 Minimum Alternative Tax (MAT) has increased to 15 percent of book profits from 10 percent. The period allowed to carry forward the tax credit under MAT was also extended from seven years to 10 years.

6. Presumptive taxation

The scheme of presumptive tax was introduced to widen the tax base as many retailers were not filing their income tax returns as they had difficulty in estimating their income tax and maintaining stock. The scope of presumptive taxation was extended to all small businesses with a
turnover up to Rs. 40 lakh. All such tax payers to have option to declare their income from business at the rate of 8 percent of their turn over and simultaneously enjoy exemption from the compliance burden of maintaining books of accounts and also they are exempted from advance tax and allowed to pay their entire tax liability from business at the time of filing their return.

7. Service Tax
Service tax was introduced by the finance act, 1994. This is an indirect tax levied on the services provided. The service provider can recover the tax from the service receiver. The tax liability shifts to the end user. 96 services were covered by the service tax act till new services were brought under the net in the 2007 budget. The service tax provider has to pay service tax at the rate of 12 Percent plus education cess of 3 percent which effectively comes to 12.36 Percent. Service Tax Act administered by Central Excise Department u/s 83 of the Finance Act. Provisions relating to the Service Tax do not extended to the state of Jammu & Kashmir. The initial exemption limit or the threshold limit has been increased from Rs. 8 lakh with effect from 1/04/08.

The New Services under the net are:

1. Stock and commodity exchanges and clearing houses
2. Asset Management firms offering unit-linked insurance plan (ULIP)
3. Customised software
4. Right to use goods, in case where VAT is not payable

Any service provided to a developer of Special Economic Zone (SEZ) or a unit in SEZ is exempt from Service tax.
8. Dividend Distribution Tax (DDT)

Dividend distributed by an Indian Company is exempt from income tax in the hands of all shareholders. The Indian Company is liable to pay DDT at 16.995 Percent (i.e. inclusive of surcharge and education cess) on such dividends.

- 28.33 Percent (inclusive of surcharge and education cess) on income distributed by a money market mutual fund or a liquid fund;
- 14.163 Percent (inclusive of surcharge and education cess) on income distributed to any person being an individual or a HUF by a fund other than a money market mutual fund or a liquid fund; and
- 22.66 Percent (inclusive of surcharge and education cess) on income distributed to any other person by a fund other than a money market mutual fund or a liquid fund.

9. Gift Tax

Gift Tax was abolished from October 1st 1998. The gifts were no longer taxable in hands of donor or donee. The finance act 2005 however amended the definition so as to provide that any sum received above Rs. 50,000 on or after September 1st 2004 by an individual or an HUF from unrelated person in cash or by way of goods & services shall be included within definition of income under section 2(24) of the IT Act and therefore be subject to tax as per section 56 of IT Act. However, on the occasion of the individual’s marriage, the entire value of gifts received will be exempted from being added to the income. Gifts received from specific relatives however continue to be exempt from tax.
10. Elimination of Standard Deduction

Under the Income-tax Act, 1961, up to the financial year 2004-05, a taxpayer was allowed a deduction of certain percentage of his/her salary income subject to a maximum amount as standard deduction in the computation of his/her salary income chargeable to income tax. This standard deduction was allowed in respect of expenditure incidental to the employment of the taxpayer. However, in order to claim the standard deduction, the tax payer was not required to prove that he had in fact incurred any expenditure for the purpose of his employment. The level of standard deduction was increased substantially over the years both in terms of percentage and overall ceiling.

It is difficult to accept that a salaried taxpayer incurs such a high part of his salary income as expenditure incidental to his employment i.e; on books and other publications necessary to perform his duties. The high level of standard deduction was often justified on the ground that unlike in the case of a self employed taxpayer, salaried employees does not have opportunities to evade taxes. As a result, the effective tax burden on salaried employee is greater than those deriving income from self employment/ business.

Therefore, the standard deduction should be viewed as compensating for loss of such ‘privilege’ and mitigating the effective tax burden. It is indeed true that a self employed tax payer has greater opportunity to evade taxes by clubbing their personal expenses with other expenses which are tax deductible. However, such lumping is often investigated and in most cases disallowed.
It is also well known that, most employers provide extensive library facilities and reimbursement to senior employees for expenditure on books and periodicals. In the case of the corporate sector, the expenditure on newspapers and periodicals is an allowable deduction without being treated as a perquisite in the hands of employee. Keeping in view the above and also recognising the considerable increase in exemption limit, standard deduction was eliminated / abolished with effect from financial year 2005-06.

11. Tax Reforms and Investment Incentives

Over the years, despite skepticism of fiscal experts over their efficiency, tax incentive package has been widely used in a variety of forms for diverse purposes. In India, a plethora of tax incentives have been built into tax law.

Tax incentives are often criticised for distorting economic activity. Incentives cause post-tax pattern of return to diverge from pre-tax pattern and therefore lead to an allocation of resources different from the efficient equilibrium which the market is supposed to generate. Tax incentives erode the tax base and thus shrink government revenue. They introduce complexity into the tax system. Incentives require definition of the eligible activities which in itself complicates tax legislation. By complicating tax laws, incentives increase the possibilities of tax evasion and litigation which in turn may adversely affect tax collections.

In case of individual assesses, tax incentives distort the incidence of tax among different taxpaying classes and hence obscure its evolution from equity angle. In fact, tax incentives distort the tax burden as suggested by statutory rates. More specifically, tax incentives reduce effective tax rates
below the statutory ones. The statutory or nominal rates may be misleading when the redistribution effect of progressive rates is considered. Up to the financial year 2004-05, India had a system called ‘Tax Rebate’. Tax rebate was a legal provision permitting taxpayers to deduct specified sums from their tax liability. Tax rebate was different from a deduction because the former was subtracted after the computation of tax liability while the later is subtracted from the income subject to tax.

Up to the financial year 2004-05, section 88 provided for rebate on tax liability to the individuals and HUFs on the amount of investments eligible for rebate. Tax rebate was deducted from tax on net income in order to arrive at net tax liability. The maximum rate of rebate was 30 percent. Also up to the financial year 2004-05, a deduction was provided under section 80L in respect of certain incomes. Section 80L was introduced by the Finance Act, 1967, originally with a view to encouraging investment in the shares of Indian companies and, perhaps, also to mitigate the double taxation of dividends for the small shareholders.

The Finance Act, 1970 substantially enlarged the scope of this section by including government securities, debentures issued by specified cooperative societies or institutions, investments in units of UTI, deposits with banking companies or co-operative banks and deposits with financial corporation’s engaged in providing long-term finance for industrial development. The scope of section 80L was also enlarged by the inclusion of National Savings Certificates (VI, VII and VIII issue), and bonds by certain public sector undertakings. The amount of deduction for the financial year 2004-05 was up to the maximum of Rs. 12,000 for incomes by way of interest on deposits, NSC interest etc. plus
an additional deduction of up to maximum of Rs. 3,000 with respect to interest on Government securities.

With effect from financial year 2005-06, tax rebate under section 88 and deduction under section 80L was replaced by a deduction under section 80C in respect of prescribed contributions to saving instruments like insurance premium, provident fund contribution, PPF, NSC etc which allow for a deduction up to the maximum of Rs. 1,00,000 from total income. This deduction is available to all individuals and payments made as premium for pension plan under section 80CCC is also included in the limit of Rs. 1,00,000. There are no sectoral caps and investments can be done in any one or more of the eligible instruments within the overall ceiling. With these amendments, now the taxpayer is allowed greater flexibility in making saving/investment decisions and the role of government is neutral between one form of saving and another.

12. Banking Cash Transaction Tax

With effect from June 1, 2005, a banking cash transaction tax was introduced and it was charged at 1 (one) per cent on withdrawal of cash on any single day from an account (other than saving account) or being receipt of cash on any single day on encashment of one or more term deposits, whether on maturity or otherwise exceeding Rs. 25,000 by an individual. Banks were required to collect the Banking Cash Transaction Tax and pay the same into government treasury by the 15th of the month immediately following the calendar month in which Banking Cash Transaction Tax was collected. Returns were also required to be filed by the bank with the tax authorities in this regard and an assessment was done by tax authorities.
The banking cash transaction tax turned out to be a boon, not for the modest revenue it brought, but for the remarkable traits that it helped to establish. Banking Cash Transaction Tax also helped the tax department to detect bogus bills, accommodation entries, artificial loss claims and dummy firms. However, Banking Cash Transaction Tax was withdrawn in the budget announced for the year 2008-09.

13. Security transaction tax

Security transaction tax was introduced to replace tax on long term capital gains from securities in the Finance Act 2004-2005 and it proposed to levy tax on transactions in securities on stock exchanges on the buyer at the rate of 0.15 percent of the value of security.

With effect from 2005-2006, a nominal increase in the rates of securities transaction tax for all categories of transactions. With effect from 2006-2007, there was an increase of 25 percent, across the board, on all rates of securities transaction tax and there was no change in the financial year 2007-2008. With effect from 2008-2009 assessment year, STT paid was treated like any other deductible expenditure against business income: levy of STT in case of options was only on premium, where the option is not exercised, liability was on the seller, where the option was exercised levy to be on the settlement price and the liability on the buyer and no changes were made in the rates of STT ie., STT was levied on the value of taxable securities by the purchaser and seller of equity shares, units of equity oriented mutual fund (delivery based ) at 0.125 percent.

On the non delivery based such securities only the seller has to pay 0.025 percent. The seller is to pay 0.17 percent on sale of derivatives and 0.25 percent on sale of unit of an equity oriented fund to the mutual fun and
there was change in the assessment year 2009-2010. Every recognised stock exchange or the prescribed person shall within the prescribed time after the end of each financial year prepare and submitted to the assessing officer in respect of all taxable securities transactions entered in to during such financial year in that stock exchange.

14. Modernising tax administration

During the financial year 2003--2004, various administrative reforms were introduced as per the recommendations of task force committee headed by Dr. Vijay Kekar, like out sourcing of non-core activities of income tax department; namely allotment of PAN etc., computer generated random selection of only two percent of the returns annually for scrutiny, direct crediting of all refunds to the bank account of the tax payer through electronic clearance system, number of forms used for the purposes of tax deduction and tax collection at source reduced from 42 to 22 pages, introduction of a one page return form for individual tax payers having income from salary, house property and interest etc., electronic filing of returns, abolition of tax clearance certificates currently needed by a person leaving India or any person submitting a tender for a government contract.

With effect from 2006-2007, the Departments of Income Tax and Customs and Central Excise has undergone by Business Process Reengineering (BPR); nationwide networks to connect 745 income tax offices in 510 cities and 550 customs and central excise offices in 245 cities, creating national databases, national data centres, data warehousing facilities and disaster recovery sites being set up, jurisdiction-free filing of returns, online tracking of status of accounts and refunds of income tax to be possible, introduction of a risk management system and Electronic
Data Interchange (EDI) in the Customs Department to reduce dwell time for cargo, E-payments of customs and excise duties to be possible, both departments to have fully computerised networks by end of 2012.

15. Sales Tax/VAT

Sales tax is levied on the sale of movable goods. Most of the Indian States have replaced Sales tax with a new Value Added Tax (VAT) from April 01, 2005. VAT is imposed on goods only and not services and it has replaced sales tax. Other indirect taxes such as excise duty, service tax etc., are not replaced by VAT. VAT is implemented at the State level by State Governments. VAT is applied on each stage of sale with a mechanism of credit for the input VAT paid. There are four slabs of VAT:

1. Zero Percent for essential commodities
2. one Percent on bullion and precious stones
3. Four Percent on industrial inputs and capital goods and items of mass consumption
4. All other items 12.5 Percent
5. Petroleum products, tobacco, liquor etc., attract higher VAT rates that vary from State to State

16. New pension scheme

Pension payments constitute an important component of committed expenditures in the Central and state budgets. The Task Force committee favoured the initiative taken by the Central Government in this context. A new pension scheme was introduced by the Central Government with effect from January 1, 2004 for Central Government employees recruited
on or after that date (except Armed Forces) replacing the defined benefit pension scheme. The TFC has recommended that the State Governments need to take up initiatives similar to those of the Central Government for pension reforms.

17. Direct Tax Code

The existing tax system is more complicated because of numerous amendments to it over the years and changes brought in to the income tax Act 1961 through various finance Acts based on the recommendations made by the various committees from time to time and judgment’s passed by the courts have made it increasingly difficult to understand and interpret. Therefore, to simplify the tax system, to minimise the litigation, broadening the tax base and eliminating the exemptions, a new bill is introduced in August 2009 popularly called Direct tax code. The Direct tax code bill seeks to consolidate and amend the law relating to all direct taxes and will replace the income tax Act, 1961.

The Direct tax code proposed to replace the income tax Act 1961, widens income tax slabs for individuals income between 2.00 to 10.00 lakh will be taxed at 10 percent between Rs. 10 lakh and Rs. 25 lakh at 20 percent and that over Rs 25.00 lakh at 30 percent. The Bill proposes to remove several tax deductions currently allowed such as those on investments in life insurance or provident funds, interest paid on housing loans shall no longer be tax deductible.

Companies will be taxed at 25 percent of business income. The Bill also imposes a minimum alternate tax of 2 percent on the assets of companies and a dividend distribution tax of 15 percent on domestic companies. Foreign companies shall pay an additional branch profits tax of 15
percent. Unincorporated bodies are taxed at 30 percent of income while non profit organisations are taxed at 15 percent of any surplus of income over expenditure. The Bill raises the wealth tax exemption limit from Rs. 15 lakh to Rs. 50 crore and widens the ambit of wealth tax to include financial assets.

18. Senior Citizens and Female Assessee’s
As an expression of gratitude to the contribution made by senior citizens (persons above 65 years of age) during their active years and taking in to account the possible hardships that they face in the advanced years of their life, tax rebate was provided to senior citizens up to Rs. 20,000 under section 88B up to the financial year 2004-2005. However, with effect from financial year 2005-2006 additional rebate under section 88B and 88C was eliminated. Now the senior citizens and female assesses get additional benefit in the form of exemption limit more than an ordinary individual. The exemption limit was Rs. 1,85,000 in the financial years 2005-2006 and 2006-2007 but in the financial year 2007-08 it is raised by Rs. 10,000 and exemption limit raised to Rs. 2,25,000 in 2008-09 and raised to Rs. 2,40,000 in the financial year 2009-2010.

Also as a token of appreciation and recognition of women as productive contributors to the economy, additional rebate of Rs. 5,000 was provided to the women tax payers (excluding senior citizens) up to the financial year 2004-2005. With effect from the financial year 2005-2006 exemption limit raised to Rs. 1,35,000 but in 2006-2007, there was no change in the exemption limit. Again, in the financial year 2007-2008 exemption limit raised to Rs. 1,45,000, but in the financial year 2008-2009 it grew to Rs. 1,80,000 and again in 2009-2010 the exemption limit raised to Rs. 1,90,000.
Conclusion

Following the macro-economic crisis in July 1991, India carried out a series of economic reforms. Tax reforms has become an integral part of the program with an objective of direct taxes has to increase overall tax revenues and shift the burden of corporate taxes to income taxes by rationalising the tax rates and exemptions, broadening of tax base and simplify the tax laws. Government’s concern with tax reforms is reflected in the appointment of a number of committees in the last few years (after 2001) to review the tax system and to suggest suitable reforms like Advisory Group on tax policy and administration for the tenth plan, Committee on review of Central Excise collection system, Expert Group on Taxation of Services, Inter-Ministerial working Group on Customs Tariff, Task force on Direct and Indirect Taxes headed by Kelkar and also introduced Direct Tax Code to replace the existing Income tax Act, 1961. Though number of committees have been constituted by the government to review taxation policy and other related issues periodically, the recommendations of the committees have not been fully implemented by the government.

Indian tax system has undergone significant changes during the last ten years (2000-2010) in keeping with the changing perception of the role of the government on rationalisation and simplification of direct taxes, improvement in taxpayer service and redesigning procedures for strengthening enforcement through the budget proposals. The major changes in the personal income tax includes exemption limit has been gradually raised, standard deduction had been withdrawn with all prevailing tax rebates removed and the 1/6th criteria for income tax assessment got modified in 2005-06. Two new taxes, the fringe benefit
tax and banking transaction tax were introduced in 2005-06, while the security transaction tax for all categories was increased by one-third. Where as in case of corporate tax, rates of taxes have been reduced and various deductions and exemptions are abolished. The minimum alternative tax has increased from 7.5 percent to 15 percent in 2009-10 etc. There have been significant attempts to improve the administration and enforcement of the tax as well through the simplification of procedures and efforts for improving efficiency of the tax administration system through computerisation, appointment of ombudsman, E-filing of returns and refunds, outsourcing of non core activities, allotment of PAN etc.