Direct Taxes Code: Super rich with over Rs 10-crore income may have to pay 35% tax

The super rich may have to pay more as the government strives to raise revenues to meet its commitment to rating agencies and markets to bring down fiscal deficit.

The government is proposing a 35% tax rate for those earning more than Rs 10 crore in the Direct Taxes Code (DTC) that is likely to be tabled in Parliament during the ongoing session. The Union Cabinet will consider the code on Thursday. The direct taxes bill, once approved by Parliament, will replace the current Income-Tax Act, which dates back to 1961.

At present, taxable income in excess of Rs. 10 lakh is taxed at 30% while those earning more than Rs 1 crore have to pay a surcharge of 10%. Further, since top earners receive substantial income by way of dividends, the Direct Taxes Code incorporates a 10% tax on dividend income in excess of 1 crore.

In the current dispensation, dividend income is tax-free in the hands of the investor as the company distributing dividends pays a dividend distribution tax at the rate of 15%.

"There can be no quarrel over taxing those earning that kind of income, but this more a symbolic gesture and does not seem like a revenue-raising move," said Sudhir Kapadia,national tax leader, EY.

Few Crorepati Taxpayers

"The government should have looked at a new design architecture for taxing dividends in the hands of recipients as dividend distribution tax adds to the overall corporate tax rate," said Sudhir Kapadia.

The corporate tax rate is proposed to be retained at 30% while the Securities Transaction Tax, which has faced vehement opposition from market participants, will stay in place.

"This will make our tax system progressive. Those earning high income should pay higher tax," a senior finance ministry official told ET.

There are only a few thousand income-tax payers that earn more than Rs 10 crore, but they account for a significant percentage of the tax paid. In 2011-12, only 1.3 lakh assessees had income in excess of Rs 20 lakh, but they accounted for 63% of the total personal income-tax collected.

Finance Minister P Chidambaram had said in his budget speech that there were only 42,800 taxpayers with income in excess of Rs 1 crore. Those earning over Rs 10 crore are likely to be a lot less, though exact numbers are not in public domain.

Many experts see these low numbers as evidence of widespread tax evasion. Political contribution of up to 5% of gross total income will be eligible for deduction.

The bill proposes to levy wealth tax at the rate 0.25% for those with assets exceeding Rs 50 crore. The new tax law, if passed by Parliament, would come into effect from April 1, 2015.

The DTC, as originally conceived by Chidambaram, had sought to radically reform and simplify the over 50-year-old Income-Tax Act by reducing tax rates to expand the base of taxpayers while doing away with exemptions. But before the draft could be made public, he moved to the home ministry.

The first draft of the DTC, released in August 2009, had suggested 10% tax on income of Rs 1.6 lakh-Rs 10 lakh, 20% on income of Rs 10 lakh-Rs 25 lakh and 30% on income beyond Rs 25 lakh in a year.

To enhance the tax base, it had suggested Exempt-Exempt-Tax (E-E-T) regime for long-term savings schemes such as the provident fund, taxing them at the time of withdrawal. Under Chidambaram's successor, the DTC underwent a complete makeover, in the process, some say, losing its basic philosophy of doing away with exemptions after lobbying by groups opposed to changes in tax benefits.

The draft underwent several changes and was substantially different from the original version unveiled by Chidambaram when it reached Parliament in the form of a bill.

A parliamentary panel headed by senior BJP leader Yashwant Sinha then recommended further changes, including major changes in the exemption limits, abolition of the Securities Transaction Tax, retaining corporate tax at 30% and area-based tax exemptions on investments.

However, though the government has accepted over 150 of the 190 suggestions made by the standing committee, it has decided not to raise the exemption limit or rejig slabs as it would have caused a Rs 60,000-crore revenue loss to the exchequer.

The standing committee had suggested that income up to Rs 3 lakh be exempt from tax, from Rs 3 lakh to Rs 10 lakh be taxed at 10%, Rs 10 lakh to Rs 20 lakh at 20%, and income over Rs 20 lakh be taxed at 30%.

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