5. A deep cut in the Corporate Taxes

Prelims Tag: Taxes and Taxation

Mains Tag: GS-III: Indian Economy and issues relating to Planning, Mobilization of Resources, Growth, Development and Employment.

Context:

- In order to revive the economy from the economic slowdown, the Finance Minister has announced a slew of major changes in corporate income tax rates. This has been made through an ordinance – the Taxation Laws (Amendment) Ordinance 2019 that amends **Income Tax Act of 1961** and the **Finance Act of 2019.**

Key provisions of the ordinance:

- The central government slashed corporate tax rates for domestic firms from 30% to 22% and for new manufacturing companies from 25% to 15% to boost economic growth.
- Effective corporate tax rate after surcharge and cess on this companies would be 25.17 percent. No Minimum Alternate Tax (MAT) applicable on such companies.
- Local companies incorporated after October 2019 and till March 2023, will pay tax at 15 percent.
- That effective tax for new companies shall be 17.01 percent, including cess and surcharge.
- Companies enjoying tax holidays would be able to avail concessional rates post the exemption period.
- MAT relief for those companies opting to continue paying surcharge and cess. MAT has been reduced to 15 percent from 18.5 percent for companies who continue to avail exemptions and incentives.
- Enhanced surcharge announced in Budget 2019 will not apply on capital gains arising on sale of any security, including derivatives by foreign portfolio investors (FPI).

Pros associated with the above move:

- Lower taxes will result in higher profit margins. This will bolster their books, and some of these companies should be able to pass on the higher margins in the form of lower product prices to consumers.
- Lower corporate income tax rates and the resultant increase in profitability of the company will definitely prompt companies to invest more, raising their capital expenditure (capex).
- Increase in the capacities of the company will eventually result in the increased employment opportunities for the youngsters.

- Given the substantially lower rates would imply that many corporates will break even much ahead than what would have been the case with the earlier rates.
- The ultimate goal of turning India into investors' darling, demonstrating the government's intent to walk the talk on economic management, restoring investors' confidence and boosting sentiments and demand will be definitely meet its success point.
- It is expected that it will give a great stimulus to 'Make in India', attract private investment from across the globe, improve the competitiveness of the private sector, create more jobs.
- The reduction in corporate tax, effectively, brings India's 'headline' corporate tax rate broadly at par with an average of 23% rate in Asian countries.

Impacts of the Rate Cut:

- The latest corporate income tax will result in the revenue foregone to the tune of Rs 1.45 lakh crore a year to the government.
- The government has set a fiscal deficit target of 3.3 percent of GDP for 2019-20. So the latest move has raised concerns of fiscal slippage, given that tax collections have been far below the budgeted estimates.

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- The new corporate income tax rates in India will be comparatively lower than USA (27 percent), Japan (30.62 percent), Brazil (34 percent), Germany (30 percent) and is similar to China (25 percent) and Korea (25 percent).
- Effective tax rate of 17 percent on newly incorporated companies in India with is almost equivalent to what corporates pay in Singapore (17 percent).

What is Revenue Foregone?

- Foregone earnings are the difference between earnings actually achieved and earnings that could have been achieved with the absence of specific fees, expenses or lost time.