<u>Understanding the Tax Structure in India: A Key Pillar of Nation-Building</u>

Taxes are the backbone of any nation's development. Governments worldwide impose taxes to fund critical projects, including infrastructure, public education, military advancements, law enforcement, and more. India has a well-developed tax structure with clearly demarcated authority between Central and State Governments and local bodies. The authority of the government to levy tax in India is derived from the Constitution of India, which allocates the power to levy taxes to the Central and State governments. In India, the tax system is designed not only to generate revenue but also to foster economic stability, promote equity, and drive national progress. In last 10-15 years, Indian taxation system has undergone tremendous reforms. The tax rates have been rationalized and tax laws have been simplified resulting in better compliance, ease of tax payment and better enforcement.

2. <u>Types of Taxes in India-</u>

The Indian tax system primarily consists of two types of taxes: **Direct Taxes** and **Indirect Taxes**.

i. <u>Direct Taxes: Taxation at the Source-</u>

Direct taxes are levied directly on individuals and corporate entities. The responsibility of paying these taxes lies solely with the taxpayer. This category of taxation is progressive, meaning the tax rate increases with income levels, ensuring a fair distribution of the tax burden. Key types of direct taxes include:

a. **Income Tax:-** Governed by the **Income Tax Act 1961**, this tax is imposed on the income of individuals and entities. Rates vary based on income slabs, making it a progressive tax. Personal income tax is levied by Central Government and is administered by Central Board of Direct taxes under Ministry of Finance in accordance with the provisions of the Income Tax Act. The rates for personal income tax are as follows:-

In India, individual taxpayers can choose between two income tax regimes: the **Old Tax Regime**, which offers various exemptions and deductions, and the **New Tax Regime**, which provides lower tax rates with limited exemptions.

New Tax Regime (Applicable for FY 2024-25 / AY 2025-26):

Annual Income (INR)	Tax Rate (%)
Up to ₹3,00,000	Nil
₹3,00,001 – ₹7,00,000	5%
₹7,00,001 – ₹10,00,000	10%
₹10,00,001 – ₹12,00,000	15%
₹12,00,001 – ₹15,00,000	20%
Above ₹15,00,000	30%

Note: A rebate under Section 87A ensures that individuals with a total income up to ₹7,00,000 pay no tax under the new regime. Additionally, the standard deduction for salaried individuals has been increased from ₹50,000 to ₹75,000.

Old Tax Regime (Applicable for FY 2024-25 / AY 2025-26):

Annual Income (INR)	Tax Rate (%)
Up to ₹2,50,000	Nil
₹2,50,001 – ₹5,00,000	5%
₹5,00,001 – ₹10,00,000	20%
Above ₹10,00,000	30%

Note: The old regime allows various exemptions and deductions, such as those under Sections 80C, 80D, and others.

Surcharge and Cess:

- **Surcharge:** Applicable on income exceeding ₹50 lakh, with rates varying based on income levels.
- **Health and Education Cess:** An additional 4% on the income tax plus surcharge.

Choosing Between the Two Regimes:

Taxpayers should evaluate both regimes to determine which is more beneficial based on their income and eligible deductions.

For further details please visit the web site of Income Tax Department at

www.incometaxindia.gov.in

b. **Corporate Tax:-** Governed by the **Income Tax Act 1961**, companies and corporate entities pay corporate tax on their income. Rates are determined annually through the Finance Act, varying by company type and turnover. Companies residents in India are taxed on their worldwide income arising from all sources in accordance with the provisions of the Income Tax Act. Non-resident corporations are essentially taxed on the income earned from a business connection in India or from other Indian sources. A corporation is deemed to be resident in India if it is incorporated in India or if it's control and management is situated entirely in India.

In India, corporate tax rates differ based on a company's residency status, turnover, and specific conditions. Here's an overview of the applicable rates for the Financial Year (FY) 2024-25 (Assessment Year 2025-26):

Domestic Companies:

1. **Standard Tax Rates:**
    - **Turnover up to ₹4 billion:** 25%
    - **Turnover exceeding ₹4 billion:** 30%

2. **Concessional Tax Rates under Specific Sections:**
    - **Section 115BAA:** Domestic companies can opt for a tax rate of 22% (plus a 10% surcharge and 4% health and education cess), resulting in an effective tax rate of 25.17%, provided they do not claim certain exemptions or incentives.

- **Section 115BAB:** New manufacturing companies incorporated on or after October 1, 2019, and commencing production before March 31, 2023, can avail a tax rate of 15% (plus a 10% surcharge and 4% cess), leading to an effective tax rate of 17.16%, subject to specific conditions.

Non-Resident (Foreign) Companies:

- **Standard Tax Rate:** 35% (plus applicable surcharge and cess).

Surcharge and Cess:

- **Surcharge for Domestic Companies:**
    - 7% on income exceeding ₹10 million and up to ₹100 million.
    - 12% on income exceeding ₹100 million.

- **Surcharge for Foreign Companies:**
    - 2% on income exceeding ₹10 million and up to ₹100 million.
    - 5% on income exceeding ₹100 million.

- **Health and Education Cess:** An additional 4% on the income tax plus surcharge, applicable to both domestic and foreign companies.

Minimum Alternate Tax (MAT):

- Applicable at 15% on book profits for companies availing certain exemptions, ensuring a minimum tax payment. However, companies opting for taxation under Sections 115BAA and 115BAB are exempt from MAT provisions.

The Finance Act, 2024, reduced the corporate tax rate for foreign companies from 40% to 35% to attract more investment.

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c. **Capital Gains Tax:- Governed by the Income Tax Act 1961,** it is a tax imposed by the government on the profit or gain that arises from the sale of a “capital asset”, such as stocks, bonds, real estate, or other investments. This tax applies in the year the transfer of the capital asset takes place. There are two types of capital gains: Short-Term Capital Gains (STCG) and Long-Term Capital Gains (LTCG), depending on the time the asset is held before being sold.held before being sold.

Classification of Capital Assets:

- **Short-Term Capital Asset:** Assets held for a period not exceeding 36 months. However, for certain assets like listed equity shares and equity-oriented mutual funds, the period is reduced to 12 months.

- **Long-Term Capital Asset:** Assets held for more than the specified short-term period.

Tax Rates for FY 2024-25 (AY 2025-26):

- **Short-Term Capital Gains (STCG):**
    - **Equity Shares and Equity-Oriented Mutual Funds:** If Securities Transaction Tax (STT) is applicable, STCG is taxed at **20%**.
    - **Other Assets:** Gains are taxed as per the individual's applicable income tax slab rates.
- **Long-Term Capital Gains (LTCG):**
    - **Equity Shares and Equity-Oriented Mutual Funds:** LTCG exceeding ₹1,25,000 is taxed at **12.5%**.

Other Assets:

- **Without Indexation Benefit:** Taxed at **12.5%**.
- **With Indexation Benefit (for assets acquired on or before July 22, 2024):** Taxed at **20%**. For land and buildings, taxpayers have the option to choose between 12.5% without indexation or 20% with indexation.

- **Key Considerations:**
- **Securities Transaction Tax (STT):** Applicable on transactions of equity shares and equity-oriented mutual funds conducted through recognized stock exchanges.
- **Advance Tax Liability:** Taxpayers are required to pay advance tax on capital gains if the tax liability exceeds ₹10,000 in a financial year.
- **Filing of Returns:** All capital gains must be reported in the Income Tax Return (ITR) for the relevant assessment year.

Exemptions:

Certain sections of the Income Tax Act provide exemptions on capital gains if specific conditions are met, such as reinvestment in specified assets:

- **Section 54:** Exemption on LTCG from the sale of residential property if the gain is reinvested in another residential property.
- **Section 54EC:** Exemption on LTCG if invested in specified bonds within six months of the sale.
- **Section 54F:** Exemption on LTCG from the sale of any asset other than a residential property if the net consideration is reinvested in a residential property.

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ii. **Indirect Taxes: Taxation Through Goods and Services**

Indirect taxes are levied on the production, sale, or consumption of goods and services. Unlike direct taxes, the burden of indirect taxes is borne by end consumers. Historically, this category included various taxes like VAT, excise duty, and entertainment tax. However, with the introduction of the **Goods and Services Tax (GST) in 2017**, India's indirect tax system underwent a transformative change.

a. **Goods and Services Tax (GST):-** The Goods and Services Tax (GST) is India's most ambitious reform in a decade_&_GST unified India's fragmented tax structure by replacing multiple indirect taxes with a simplified regime. It eliminated the cascading effect of taxation, significantly reducing the cost of goods and services. GST is categorized into:

Central GST (CGST): Levied on **intra-state sales**, collected by the Central Government.

State GST (SGST): Levied on **intra-state sales**, collected by State Governments.

Integrated GST (IGST): Levied on **inter-state sales**, collected by the Central Government.

Unified Tax Structure:

- GST has subsumed multiple taxes like excise duty, service tax, VAT, CST, octroi, and luxury tax.
- It eliminates cascading effects (tax on tax).
- Businesses with annual turnover exceeding ₹4 million (₹2 million for services) must register for GST.
- Special thresholds apply for northeastern and hilly states.

GST Council:

- Apex decision-making body for GST in India.
- Comprises the **Union Finance Minister (chairperson) and finance ministers of states.**

GST Rates in India: The GST Council has categorized goods and services into the following tax slabs:

- **0% (Nil):** Essential goods like milk, eggs, unprocessed food, and books.
- **5%:** Basic goods like edible oils, sugar, and essential medicines.
- **12%:** Processed foods, smart phones, and some medical devices.
- **18%:** Majority of goods and services, including hair oil, toothpaste, and consumer electronics.
- **28%:** Luxury goods and sin items like high-end cars, tobacco, and aerated drinks.
- **Additional Cess:** On luxury and sin goods, calculated over the 28% rate.

Special Schemes Under GST:

Composition Scheme:

- Small businesses with a turnover of up to ₹15 million can opt to pay a fixed GST rate (1% for traders, 5% for restaurants) instead of regular GST.

Reverse Charge Mechanism (RCM):

- GST is paid by the recipient of goods/services instead of the supplier in certain notified cases.

For further details please visit the web site of GST India at

https://www.gst.gov.in

b. **Custom Duty:** It is an indirect tax levied on goods imported into or exported out of the country. The primary objective of customs duty is to regulate the movement of goods across borders, protect domestic industries, and generate revenue for the government. This is levied by the Central Government. The **Customs Act, 1962** governs the levy, collection, and enforcement of customs duties in India. Customs tariffs are prescribed under the **Customs Tariff Act, 1975**. Vary depending on the nature of the goods, their classification under the **Harmonized System of Nomenclature (HSN)**, and the trade agreements between India and other countries. Preferential rates apply under **Free Trade Agreements (FTAs)**, such as those with ASEAN, Japan, and South Korea.

Types of Customs Duty:

- **Basic Customs Duty (BCD):** Levied on all imported goods at rates specified in the Customs Tariff Act. Rates typically range from 5% to 40%.
- **Integrated GST (IGST):** Applied on imports to ensure parity with domestic goods, aligning with GST laws.
- **Social Welfare Surcharge (SWS):** Levied at 10% of the Basic Customs Duty to fund social welfare schemes.
- **Safeguard Duty:** Imposed on goods to protect domestic industries from an unexpected surge in imports.
- **Anti-Dumping Duty:** Applied to imported goods sold below fair market value to protect domestic industries from dumping.
- **Countervailing Duty (CVD):** Levied to counter subsidies provided by exporting countries to their exporters.
- **Customs Cess:** Additional charges on certain goods to fund specific government initiatives.

Import Duty Structure:

- The **effective customs duty** on imports is a combination of:
    - Basic Customs Duty (BCD)

- IGST
- Social Welfare Surcharge (SWS)
- Additional duties like Anti-Dumping, Safeguard, or CVD (if applicable).

Export Duty:

- Imposed on select goods such as petroleum products, iron ore, and certain agricultural commodities to discourage their export and ensure domestic availability.

Customs Duty Exemptions and Concessions:

Exemptions for Specific Goods:

- Raw materials for manufacturing.
- Goods imported for research and development.
- Imports under bonded warehouse facilities.

Duty Drawback Scheme:

- Exporters can claim a refund of customs duties paid on imported inputs used for exported goods.

Key Considerations for Importers/Exporters:

Customs Classification:

- Accurate classification under HSN codes is critical to determine applicable duties.

Valuation Rules:

- Customs duty is calculated based on the **Transaction Value** (CIF: Cost, Insurance, Freight).

Customs Clearance:

- Importers/exporters must comply with procedures for filing **Bill of Entry** (imports) and **Shipping Bill** (exports).

Trade Agreements:

- Importers can avail reduced duty rates under FTAs by providing certificates of origin.

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c. **The Central Excise Duty (CED):** It is an indirect tax placed on items made in India and intended for domestic use. The taxable event is manufacture,' and central excise duty liability begins when the items are made. It is a manufacturing tax paid by the manufacturer and then passed on to the customers. The duty is governed by the **Central Excise Act, 1944**, and the **Central Excise**

Tariff Act, 1985. Central Excise Duty is imposed on goods manufactured or produced within India, excluding items produced in Special Economic Zones (SEZs). The duty becomes payable upon the removal of goods from the place of manufacture. Most of it is subsumed in GST except for the following products:

- Crude petroleum
- Diesel with a high rate of acceleration
- Spirit of motion (commonly known as petrol)
- Natural gas is a renewable energy source.
- Fuel for aviation turbines
- Tobacco and tobacco products

These items are specified in the Union List under the Seventh Schedule of the Indian Constitution, granting the central government the authority to levy excise duties on them.

Types of Excise Duty:

- **Basic Excise Duty (BED):** Also known as the **Central Value Added Tax (CENVAT)**, levied under Section 3 of the Central Excise Act, 1944, on all excisable goods except salt.

- **Special Excise Duty (SED):** Imposed on special goods classified under the Second Schedule of the Central Excise Tariff Act, 1985.

- **Additional Excise Duty (AED):** Levied on goods of special importance under the Additional Duties of Excise (Goods of Special Importance) Act, 1957.

- **Taxable Event:** The manufacture or production of excisable goods is the taxable event, and the duty is typically paid by the manufacturer.

Central Excise Duty Rates:

The rates for central excise duty on petroleum products and tobacco are specified by the central government and are revised periodically based on fiscal and economic needs. Examples include:

1. **Petroleum Products:**
    - **Petrol (Unbranded):** Excise duty of ₹19.90 per liter (as of recent revisions).
    - **Diesel (Unbranded):** Excise duty of ₹15.80 per liter.
    - **Branded Petrol and Diesel:** Slightly higher rates apply.

2. **Tobacco Products:**
    - Excise duty varies based on the type of tobacco product (cigarettes, bidis, chewing tobacco, etc.) and its length or weight.

Note: These rates are subject to frequent changes, particularly during budget announcements or when the government adjusts duties to manage inflation or revenue requirements.

Exemptions and Concessions:

- Small-scale industries with an annual turnover below a certain threshold are exempt from central excise duty.
- Goods exported from India are exempt from excise duty to promote exports.

Recent Developments:

- In **2024**, the government revised excise duties on petrol and diesel as part of its fiscal policy to manage inflation and revenue generation.
- The **Agriculture Infrastructure and Development Cess (AIDC)** on petrol and diesel continues to fund rural and agricultural projects.

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