VIEW AND COUNTERVIEW

DO WE NEED A NEW INCOME TAX LAW?

There are at least two views, if not more, on almost everything. Call it perspectives or facets. VIEW and COUNTERVIEW seeks to bring before a reader, two opposite sides of a current issue and everything in between. Our world is increasingly becoming linear and bipolar. VIEW and COUNTERVIEW aims to inform the reader of multidimensional totality of an issue, to enable him to see a matter from a broad horizon.

This first 'VIEW and COUNTERVIEW' is on Direct Taxes Code (DTC). Another attempt to resurrect the DTC has recently gained momentum. Since its first appearance in 2009, a new DTC is meant to serve many purposes - to amend and consolidate the law, simplify language, provide stability and replace the Income Tax Act, 1961 (ITA).

VIEW: WE DON'T NEED A NEW TAX LAW

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The Government proposal to have a completely new income tax law is based primarily on two premises – that the old law has outlived its useful life, and that the existing law is too complex. Is this really correct?

The ITA probably holds the world record for the most amended law in the world. Every year, there have been more than 100 amendments to the law through the Finance Act, and in some years, we have also seen an Amendment Act. Therefore, the changes to the law have ensured that it kept pace with the changes that the Government thought it required from time to time. In a sense, it is therefore not an old law – probably more than 30% of it is less than 10 or 15 years old.

Is the ITA too complex? No one can deny that it is certainly complex. But why is it so? It is because the Government made changes to it every year in a haphazard manner, trying to plug every loophole. Very often, the amendments have been made without taking into account other provisions which were already in existence. Further, the drafting of the amendments has not been up to the mark, leaving many ambiguities in the law.

Would a new income tax law really solve all these problems? One hopes that a new law may perhaps be more consistent, all the provisions being drafted at the same time.

If we compare the laws drafted in the 19th century, such as the Indian Contract Act, 1872 or the Indian Trusts Act, 1882, one finds the quality of drafting of those laws far superior to laws drafted in recent times. These laws have stood the test of time. The old laws would give a broad framework, or principles, on which every transaction is to be tested, without trying to cover each and every situation separately. In the amendments to the tax laws, the approach has been a rules based approach, making specific provisions for different types of situations, leaving uncertainty about other situations, which results in litigation.

Given the poor quality of drafting of our tax laws in recent times, it is more likely that we would end up with a new law which is more badly drafted than our existing law. Further, if the new law is also amended every year with more than 100 amendments, as in the past, no purpose would be served at all, and the new law would also soon become as bad as, if not worse than, our existing income tax law. Worse still, we may end up with a law like the GST law, with scores of amendments every month just to remove the anomalies!

The broad structure of our existing income tax law has been in existence for almost a century, and is well

understood by most taxpayers. If structural changes are made, there are likely to be more tax defaults due to time taken by taxpayers all over the country to understand the new conceptual changes. Unless such initial tax defaults are condoned, a large number of taxpayers could end up facing penalty and prosecution.

Today, we are in a situation where there is clarity on 90% of our tax law provisions. Given the extensive litigation, and the large number of decisions of the Supreme Court and the High Court on income tax matters, the law is settled on most issues. Further, the circulars issued by the CBDT from time to time, have also clarified many of the issues. A new tax law with different language will, in all probability, result in unsettling all these issues. Given the fact that our courts are barely able to cope with tax litigation on 10% of the issues, there is likely to be an explosion in the quantum of tax litigation, which our judicial system may be incapable of handling. Further, it would take years for the CBDT to issue clarifications on so many issues, which would result in litigation in the meanwhile.

Given the past history of the draft DTC and the non-implementation of most of the recommendations of the Easwar Committee and earlier committees, new tax laws or amendments have tended to be biased in favour of the revenue, and have ignored taxpayer-friendly recommendations. It is therefore highly likely that the new tax law may also not be very taxpayer-friendly. In the DTC, an attempt was made to project it as taxpayer-friendly by proposing reduced tax rates. However, this was more than neutralised by provisions seeking to tax an artificially higher income. As the past experience shows, tax rates can be easily hiked, and therefore, ultimately the taxpayer may end up with the worst of both worlds - a higher taxable income, as well as the same, if not higher, tax rates.

A new tax law will result in large scale disruption of economic activity. A large amount of business resources will have to be dedicated to understanding the new law, changing business processes to comply with the new law, and educating all levels of business about the new tax requirements. This will definitely result in a slowdown in business growth in the short term – a slowdown which the country can ill afford. One has already seen the impact of the GST law on the country's economic growth. Another new tax law in such a short time span has the potential to further cripple the economy.

Many taxpayers have made long term commitments relating to their investments (such as, opened a 15 year Public Provident Fund account, or taken a 20 year life insurance policy), based on existing tax laws. If significant changes are made to the tax laws in relation to such investments, it would cause significant losses to taxpayers on account of their having to terminate such investments, or pay tax in respect of such investments.

What is needed is not a new income tax law, but a new taxpayer and business friendly approach of the tax department and tax authorities. The existing law can easily be amended to simplify it– most of the complications have arisen due to amendments made, on account of misconceptions or lack of understanding of commercial reality by the tax authorities. This would cause far less disruption and turmoil in business and the economy.

A new attitudinal approach by tax authorities is essential – every taxpayer should not be regarded as a potential tax evader, but as a compliant citizen, unless the facts clearly indicate otherwise. Defaults are often due to other genuine factors, not necessarily due to an attitude of non-compliance. Retraining of tax officers is therefore essential to inculcate this attitude.

This is what the country needs rather than a new tax law – rationalisation and simplification of the existing income tax law, with reorientation of the attitude of tax officers.

COUNTERVIEW: YES, WE NEED A NEW CODE

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"They won't listen, do you know why? Because they have certain fixed notions about the past. Any change would be blasphemy in their eyes, even if it were truth. They don't want the truth. They want their traditions." - Isaac Asimov

It is intriguing, if not unfortunate, that we are debating the need to have a new code or not, instead of devoting our limited energy in shaping and designing the legislation whose need is inevitable; not because it may do wonders for us but because the present prescription has reached a rotten stage and its stench is overpowering and without

doubt requires to be given a burial that is due to it. Ask anyone who has remotely to deal with the ITA and he would waste no time and spare no words in expressing his frustration in the choicest words. It is foolhardy to ascribe the dismal stage of affairs to the lack of administration and accountability, alone and even if it were to be true, it is the ITA and its deceptive and fundamental fallacies in the basics including in respect of the concepts of the income and deductions that have allowed the inefficient and corrupt to proliferate without any checks. The need for the Code is examined and approved by not less than three Finance Ministers, over a period of almost a decade, and by the legislature, too, after a detailed report of the joint parliamentary committee that was issued after the due consideration of the suggestions of all concerned with the income tax.

Eminent jurists N. A. Palkhivala and B. A. Palkhivala in their preface to the eighth edition of the book 'The Law and Practice of Income tax' write: *"today the Income tax Act, 1961, is a national disgrace. There is no other instance in Indian jurisprudence of an Act mutilated by more than 3300 amendments in less than 30 years."* This was written on 21st February, 1990 and since then more than 28 Finance Bills were presented till 2018. These Bills have introduced at least 2700 amendments, since then, to reach the unpardonable figure of 6000; think of a human body which has been operated for more than 6000 times. Again Palkhivalas in 1990 say, in the context of the Act, *"the tragedy of India is the tragedy of waste-waste of national time, energy and manpower, tens of millions of man hours, crammed with intelligence and knowledge of tax gatherers, tax payers and tax advisers are squandered every year in grappling with the torrential spate of mindless amendments. The feverish activity achieves no better than fever."*

It is essential to clinically examine the need for the new Code in place of the ITA. This can be best done by examining step by step, whether the present law has been able to deliver all that what is expected of a good revenue law especially in the areas of clarity, *stability, accountability, lower susceptibility to litigation, prevention of evasion and money laundering, settlement of disputes, booking the offenders, widening the tax base, simplicity, easy compliance, transparency, digitalization, data security,* and a few more. Let us see whether each of the above tests and a few more are met by the ITA.

Prevention of evasion and money laundering: An important objective of any revenue law is to quickly bring to book the offenders by putting in place the deterrent provisions that can be effectively administered with precision without permitting any discretion. Rampant cases of fictitious shell companies, bogus purchases and expenditures, penny stocks, gifts, accommodation entries and overseas and domestic round tripping are a few examples of abuses that have flourished with impunity the courts have found laws to be inadequate to book the offences and the offenders. This is one of the single most failures of the ITA.

Investigation and results of investigation: While the ITA gives power of investigation to authorities it is lacking in enabling the authorities in converting the findings of the investigation into bringing the unaccounted funds to tax and punishing the offenders. There is ineffective and confused mechanism for assessment of the income and wealth found as a result of tiresome investigations. The chapters dealing with the block assessment and special assessment of search cases are the examples of such cases.

Settlement of disputes: The ITA lacks effective mechanism for a quick, effective and judicious settlement of disputes. The functioning of the settlement commission has not been very inspiring and the commission does not command the respect of the framers of the law as is evident from the flip flops in these provisions in the last decade.

Prosecuting the offenders: There are less than 1000 cases of successful prosecutions in the 57 years history of the ITA. The provisions for penalty, though numerous have not commanded the serious respect from tax payers and even tax gatherers; they have not provided any effective deterrence for the offenders.

Accountability: The provisions have been found to be regularly abused. There are virtually no provisions in the Income tax Act to publicly book the administrators for deliberate abuse of the law to suit their ulterior motives. The lack of these provisions is believed to be the single most factor in proliferation of rampant corruption in administration of law.

Clarity for clutter: The Act, is replete with provisions that are highly ambiguous and demand clarity. Income,

revenue and capital, characterisation of income method of accounting, taxable event, time and year of taxation, explanations, provisos, residential status, tax status SAAR, MAT, GAAR, prospectivity, etc. are the example of cases on which no clarity is possible under the Act. Even the highest court of the land had time and again expressed its anguish over a highly perplex tax law. Hundreds of explanations and provisos, inserted after the main provisions, in the name of clarifications, have in effect made the present Act one of the most incomprehensible and vague piece of legislation. Some of the sections have more than 15 provisos.

Stability: ITA has been compared with a railway ticket, good only for one journey and sometimes not even for the whole journey. Not once but on several occasions, the tax payers, domestic and foreign, have found the Act to be devoid of any stability and the incessant amendments to be destabilising more so in cases when the changes seek to overturn the well considered decisions of the courts.

Retrospective application: Amendments are introduced, with retrospective effect. These amendments are introduced in the name of clarification. In many cases, the amendments are applied retrospectively though they have been expressly introduced with prospective effect. Then there are cases of amendments, which have unintended retroactive application. This leads to reopening and revisions and in extreme cases rectifications. Every third case, before the courts, deal with such issues of the effective date of application of the law.

Non alignment with Tax Treaties: There is a strong case for introduction of clear and unambiguous provisions to ensure that there is little or no mismatch with the treaties signed by India with open eyes. Likewise, a great deal of work is required on Transfer Pricing regulations to check the enormous level of litigation surrounding them. The country with the growth aspirations cannot afford the proliferation of ill conceived assessments. At the same time the new provisions are required to prevent leakage of lawful revenue which is presently lost on account of the technical infirmities. Experience suggests that the administrative measures alone are not helpful to check these deficiencies and statutory support is called for in this direction.

Compliance provisions: More than two third of the provisions of ITA deal with compliance and regulation. Stringent provisions are available in the Act to penalize and even punish assessees carrying out governmental work in the name of compliance. These days the provisions are seen to be abused by issuance of numerous notices for prosecuting unsuspecting citizens for trivial offences. Detailed provisions are required to minimize the compliance burden and restrict abuse of power by the tax authorities.

Unorganised and unstructured placement: Sections of the ITA are arranged numerically as also alphabetically. Even chapters of the Act are arranged alphabetically besides being numbered. All of these have made the Act into a chaotic and overwhelming piece of legislation leaving the reader helpless. There is a great need to organize and present the provisions for facilitating a cohesive and constructive reading.

Information and Income tax security: There is an urgent need to ensure the security of the massive data collected by the Income tax Department. Recent cases of large scale misappropriation of funds by refund claims of TDS and GST and the cases of bogus tax credits are the examples of lack of IT security. It is the obligation of those who collect details in the name of the Income tax Act. Specific provisions are required in law to make the Government accountable for even a smallest leakage and to penalise and punish those responsible for breach of the faith reposed by the citizens in them.

Tax Administration: Best laws are opposed when administered poorly and the bad laws, administered with compassion, are tolerated. There cannot be two views that there remains a great deal of dissatisfaction about the manner in which the law is administered. Lawful claims of the tax payers are delayed or rejected and in many cases frustrated. While making the authority accountable is a solution in the right direction, it is required that express provisions are made in law to ensure a well-oiled and efficient tax administration that empowers the tax payers to book the authorities for their ill-conceived actions.

Equity and Fairness and Neutrality: At times the provisions of the Act have been found to be unequitous or unfair to a class of persons. For example, there is a discrimination between residents and non-residents, for and against, in many provisions of the Act. Such discrimination has led to an unending litigation and requires to be corrected by the express provisions of law.

Transparency: There is a near unanimity in the view that the Income tax Department, as a rule, has failed to provide the copies of the material garnered or statements recorded by them and used in assessment. There is a great deal of resistance in sharing the reasons for reopening, audit objections and proceeding sheets. The authorities have been admonished by the courts for their diffidence but the same has not been able to check their approach. Express provisions alone can make them comply with the provisions of natural justice.

Generally: Introduction of provisions in law to ensure that the administrative cost of tax collection is pegged at the desired percentage of the collection will be a step in the right direction. There is a fear that this cost one day will outgrow the revenue collected and thereby denying the Government of the adequate revenue which it should get as a result of entire exercise. Provisions are required for ensuring convenience in payment of taxes and generating full credit for such payments and for instant refund of excess taxes paid. Existing provisions are found to be inadequate for achieving these and a few other objectives.

Finally, it will be childlike to believe that the introduction of the new Code by itself will bring the much desired clarity and efficiency and will usher the country in to a state of bliss. Legislating a good code, with all its trappings, may not do much good if its implementation is not actively monitored and its principles are not fiercely safeguarded by all of us. ■