# THE INDIAN TAX SYSTEM AS A FACTOR OF BUSINESS COMPETITIVENESS

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***ABSTRACT***
*This paper seeks to study the corporate income tax law's specifics of Indian companies and understand if it can to constitute a competitiveness factor for these businesses. The research makes a legal structure analysis of India Jurisdiction, it incorporates several Indian data sources: the Constitution of India and the Income-Tax Act of 1961. The results show that the Indian lawmaker is conservative on legislative changes. The law regulating the taxation of corporate profits dates back to 1961, and despite some amendments, it maintains over time. The fact that corporate tax rules remain stable over time represents predictability for investors, which is a very compelling competitiveness factor for business. However, this law presents some less positive features in some situations. The wording's law is old, so sometimes it is challenging to interpret the legislator intention; it can means difficulties in compliance's law. Also, the law establishes particular rules for taxable bases' determination on income tax corporate. It represents a duplication of accounting and tax rules, so, each entity has to prepare accounting and a tax statement.*
***Keywords:*** *India, Tax System, Corporate Income Tax Law, Income-Tax Act*

## 1. INTRODUCTION
According to the last estimates of the United Nations, currently, India is the second-most populous country in the world, representing 17,71% of the entire worldwide. Only China surpasses India, representing 18.59% of the world's population[1]. Beyond the population dimension, it has gone noticed in the economic dimension. Recently, it passed assume to take a privileged economic position, managing to transcend significant economies with a stable economic position. According to the International Monetary Fund, in 2018, this country presents a Gross Domestic Product (GPD) growth rate of 7,3%[2]. In the opinion of Barro (1997), the growth rate is increasing by "enhanced by higher initial schooling and life expectancy, lower fertility, lower government consumption, better maintenance of the rule of law, lower inflation, and improvements in terms of trade". Relating to the maintenance of the rule of law, Knack and Keefer (1997) studies the countries' subjective indices. It includes the "quality of the bureaucracy, political corruption, likelihood of government repudiation of contracts, risk of government expropriation, and overall maintenance of the rule of law". The preservation of the rule of law does not ignore tax domain because jurisdiction needs revenues collection to finance public expenditure. Thus, scholars keep interested in to research the relationship between tax systems and economic growth (Reis and Ramos, 2014). Nabais (1998) defends persons, individual or legal ones, have a fundamental duty to pay taxes, it justifies the taxation of corporate income. Income-tax Act (ITA) regulates the taxation of Indian companies' incomes. In this context, business entities are taxpayers in this tax jurisdiction alongside individual people.

*Table following on the next page*

[1] https://www.worldometers.info/world-population/population-by-country/, consulted September 12, 2019.
[2] https://www.imf.org/en/Countries/IND#whatsnew

*Table 1: Direct Tax Collection of India*

(Rs. in crore)

| Financial Year | Corporate Tax | Personal Income Tax@ | Other Direct Tax | Total |
|---|---|---|---|---|
| 2000-01 | 35696 | 31764 | 845 | 68305 |
| 2001-02 | 36609 | 32004 | 585 | 69198 |
| 2002-03 | 46172 | 36866 | 50 | 83088 |
| 2003-04 | 63562 | 41386 | 140 | 105088 |
| 2004-05 | 82680 | 49268 | 823 | 132771 |
| 2005-06 | 101277 | 63689 | 250 | 165216 |
| 2006-07 | 144318 | 85623 | 240 | 230181 |
| 2007-08 | 193561 | 120429 | 340 | 314330 |
| 2008-09 | 213395 | 120034 | 389 | 333818 |
| 2009-10 | 244725 | 132833 | 505 | 378063 |
| 2010-11 | 298688 | 146258 | 1049 | 445995 |
| 2011-12 | 322816 | 170181 | 990 | 493987 |
| 2012-13 | 356326 | 201840 | 823 | 558989 |
| 2013-14 | 394678 | 242888 | 1030 | 638596 |
| 2014-15 | 428925 | 265772 | 1095 | 695792 |
| 2015-16 | 453228 | 287637 | 1079 | 741945 |
| 2016-17 | 484924 | 349503 | 15286 | 849713 |
| 2017-18* | 571202 | 419998 | 11541 | 1002741 |

*Source: Union Finance Accounts of respective years and reports of C&AG/Receipt Budget. Cited in: INCOME TAX DEPARTMENT OF INDIA Time Series Data, Financial Year 2000-01 to 2017-18.*

Table 2 presents the evolution of taxpayers' numbers in India in the last five assessment years. It shows all the taxpayers' categories (Aldeia). During the period analysed, "individual" taxpayers represented approximately 94% each of the five-assessment years. In the same time, "company" and "firm" taxpayers represent nearly 3% of the total taxpayers' number. In AY 2017-18, the total of taxable entities amounted to 74,127,250. The direct tax collection of India, between YA 2000-01 and YA 2017-18 (table 1), consistently shows that corporate tax supports the major part of direct tax revenues, reaching 67% of total revenues in YA 2010-11. This result has been declining in recent years, achieving the value of the 571 202 Rs in YA 2017-18, which still means 57%. Those data allow an understanding that corporate income is the biggest responsible for the Indian direct tax revenues, even though, corporate taxpayers are much smaller than individuals’ ones.

*Table 2: Number of taxpayers*

| Category | AY 2013-14 | AY 2014-15 | AY 2015-16 | AY 2016-17 | AY 2017-18 |
|---|---|---|---|---|---|
| AOP | 141,533 | 160,116 | 180,715 | 205,598 | 224,399 |
| BOI | 6,304 | 7,077 | 7,518 | 8,687 | 9,290 |
| COMPANY | 704,473 | 748,173 | 769,425 | 811,309 | 838,174 |
| FIRM | 1,042,649 | 1,092,692 | 1,161,163 | 1,254,193 | 1,316,305 |
| GOVERNMENT | 240 | 357 | 510 | 763 | 1,313 |
| HUF | 964,277 | 1,003,089 | 1,058,504 | 1,121,578 | 1,136,853 |
| AJP | 10,273 | 10,629 | 11,146 | 11,720 | 11,501 |
| LOCAL AUTHORITY | 6,027 | 7,188 | 7,591 | 8,356 | 9,093 |
| INDIVIDUAL | 49,711,477 | 53,911,494 | 58,094,614 | 65,598,364 | 70,319,448 |
| AOP(TRUST) | 206,289 | 217,996 | 232,513 | 253,266 | 260,874 |
| **TOTAL** | **52,793,542** | **57,158,811** | **61,523,699** | **69,273,834** | **74,127,250** |

*Source: INCOME TAX DEPARTMENT OF INDIA Time Series Data, Financial Year 2000-01 to 2017-18*

The Indian economy's particularities and the fact journals not deal it sufficiently, have been arousing the interest of scholars. Almost all the research about Indian' economy appears in the last decade (Chaudhuri et al., 2006, Nayar, 2011, D. V and Rathod, 2015, Nithin and Roy, 2016, Handy and Kirkpatrick, 2016, Chugh and Cropper, 2017, Ahmed, 2018, Sohrabji, 2019). In particular, Green and Murinde (2008) research the impact of tax policy on corporate debt of India; Deven et al. (2017) related income inequality to fiscal policy and economic growth; and, more recently Neog (2019) understood if tax spending helps to promote India's growth. Even though some recent studies to relate tax policy with Indian economic growth, it is possible to conclude the theme is still unexplored and to the best of our knowledge, there are no studies with the investigation about corporate income tax in India as a competitiveness factor. In particular, there is needed to understand better how India taxes corporate income, and if this legal rule constitutes a competitive factor for Indian companies. This research addresses this gap by analysing the legal dispositions that approach the direct tax of India. The research questions by the paper are i) How are corporate income tax characteristics in India? Also, ii) Constitutes those characteristics a competitive factor for Indian companies? For this purpose, this paper examined the legal norms of India. Four sections compose this paper. The introduction, in the first, it makes theme framework, it presents the justification, issue, methodology and goals of the research. In the second section, it analyses the researches theoretical background. After, in the third section, studies the corporate income taxation in Indian tax jurisdiction. Moreover, finally, the conclusions.

## 2. TAX SYSTEMS AND ECONOMIC GROWTH

Endogenous growth theory stands economic growth is principally the effect of endogenous and non-endogenous influences, and it means external ones. It holds that the investment (human capital, knowledge and innovation) support the economic growth substantially. It also argues that the long-term growth rate of an economy is dependent on economic policies (Barro, 1990).

Hindriks and Myles (2013) consider that a tax policy that promotes savings affects long-term equilibrium, it improves the capital/labour ratio, that maximises per capita consumption. Reis and Ramos (2014) note that in the context of economic growth models, conclusions are consistent that the possibility of saving-oriented fiscal measures could contribute to sustained economic growth as they allow capital accumulation. The author also points out the effects of taxation on economic growth, which can be negative or positive. Negative, because given that taxation influences the choices of economic agents, which impairs the growth of an economy. Positive, as the realisation of certain public expenditures and the provision of some public goods, can positively affect economic growth, given the qualitative improvement of existing factors of production or the introduction of new factors. This opposition to the effects implies the existence of an optimum dimension of taxation, Hindriks and Myles (2013) demonstrate this relationship. It means that the increase in the level of taxation must imply an increase in the quality of spending; this idea is underlying the economic legitimacy for tax collection (Reis and Ramos, 2014). Studies investigate the relationship between taxation and economic growth (Barro, 1991, Plosser, 1992, King and Rebelo, 1990, Bergh and Henrekson, 2011, Colombier, 2015), in general, they consider that there is a negative relationship between the level of taxation and economic growth, although this understanding is not consensual among economists. Thus, the characteristics of tax systems and the way they are structured are particularly relevant in the economic field. Fairness, efficiency and simplicity are the desirable tax systems' characteristics. A simple tax system is attractive to taxpayers and tax authorities. Simplicity allows less doubt about the correct application of tax law, implies individuals and companies to spend less time in fulfilling tax duties, and makes the system less contentious due to the less complicated regulatory provisions that constitute it (Martins, 2005). At the level of tax competition, the need for simplification of tax systems is mainly claimed to simplify business taxation so that they pay less and more efficiently, as global economic competition is not sympathetic. With ultra-complex tax systems as they tend to be today (Nabais, 2008). Therefore, simplicity is an essential condition for the proper tax system's functioning. Usually, it implies i) greater security and certainty for taxpayers; ii) to tax authority, it represents lower administrative costs for the implementation and monitoring of developed tax policies as well as lower system management costs; and iii) to the taxpayer, it means lower compliance costs (d'Oliveira Martins, 2015). In this conceptual background, this research aims to address two questions:

1) How are corporate income tax characteristics in India?
2) Constitutes those attributes a competitive factor for Indian companies?

*Figure 1: Legal structure analysis of India Jurisdiction*

| | India Tax System | |
|---|---|---|
| Supreme Law | Constitution of India<br>Constituent Assembly of India on 26 November 1949 | |
| Corporate income taxation law | Income-Tax Law of 1961<br>Act 43 of 1961, Parliament of India | |

In order to answer them, it makes a legal structure analysis of India Jurisdiction. It includes some Indian data sources: The Constitution of India and The Income-Tax Act of 1961.

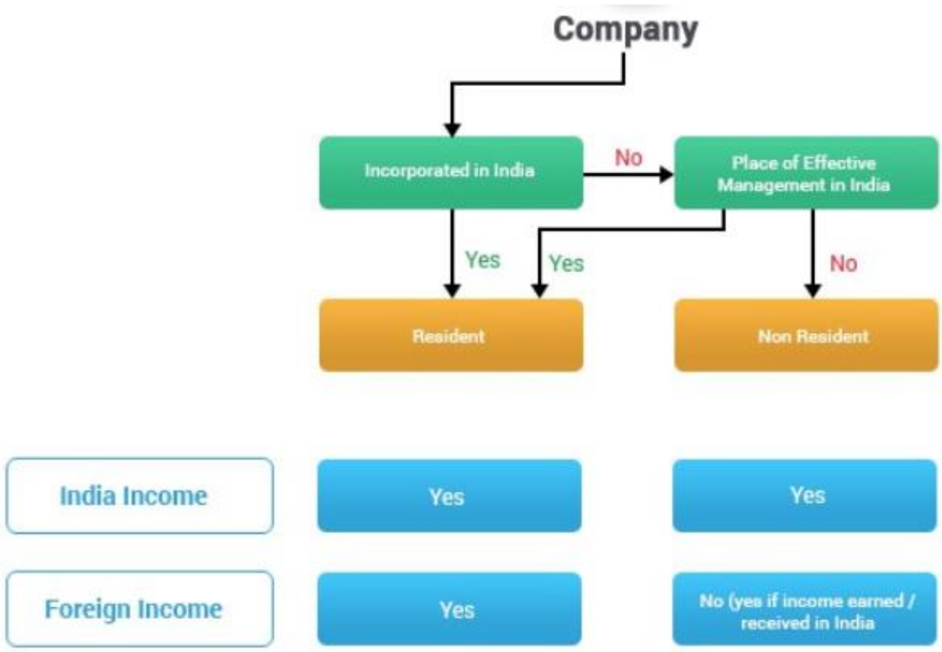
## 3. THE INDIA TAX SYSTEM

India's Supreme Law is the Constitution of India[3] (CI), the Constituent Assembly of India introduces it on 26 November 1949. Until this moment, it continues to be an amendment, already occurred 103 alterations, and the last one was in January 2019, known as the Constitution Act, 2019. The constitutional framework of India tax system is brief. In Chapter I, Finance, of Part XII - Finance, property, contracts and suits, of the CI treats tax questions. Article 265 introduces the theme of " Taxes not to be imposed save by authority of law". It determines "no tax shall be levied or collected except by authority of law". Although several amendments to the Supreme Law, article 265 never suffered a change. This legal disposition imposes to the taxes' collection to the legal forecast, it means, it is underlying the principle of legality, the fundamental principle of constitutional tax law. According to Jarach (1957), this is because the tributes represent invasions of the public power in the private riches and a Rule of Law, these invasions must be made only by legal instrument. This rule set the legality's principle as the base of Indian Tax System similar to other European tax jurisdictions such as Spain (Lapatza, 1992, Aldeia, 2017) in article 31 of the Spanish Constitution[4]; or Portugal (Dourado, 2007, Nabais, 2002, Xavier, 1978), in the article 103 of the Portuguese Supreme Law[5]. The Income Tax Act (ITA) of 1961 regulates the Indian income taxation of individuals and companies. In section 4, paragraphs 1 establishes this rule burden the total income of every person. Section 2(31) explains whom they are the taxpayers: "an individual, an undivided Hindu family, a company, a firm, an association of persons or a body of individuals, whether incorporated or not, local authority and every artificial juridical person, not falling within any of the preceding sub-clauses". So, this legislation predicts also the taxation of companies' incomes. Section 5 of the same law determines the Act's ambit. To the resident business, are taxes all the income, regardless of the source. To foreign entities, the taxation occurs over indiscriminate source income received or deemed from India (Figure 2), taking into consideration the territory principle (Xavier, 2011). Disposition of section 6(3) clarifies the determination of Companies residence, it means, a company is resident in India if it is an Indian company; or its place of effective management, in that year, is in India, it means the place where happen the crucial necessary management and commercial decisions for the business' conduction as a whole. In addition, and relating to incomes taxed under this legal disposition, the section 2(22A) clarifies the concept of "domestic company", it represents the Indian company or other that has met the requirements of this law for the declaration and payment, in India, of the dividends payable out of such income. In opposition to the domestic company, the income law also predicts, in section 2(23A), the concept of "foreign company", it means a company which is not a domestic company.

*Figure following on the next page*

[3] https://www.india.gov.in/sites/upload_files/npi/files/coi_part_full.pdf
[4] *Constitución Española.*
[5] *Constituição da República Portuguesa*

*Figure 2: Companies taxation*




*Source: https://www.investindia.gov.in/taxation, consulted on September 7, 2019.*

Furthermore, the Act explains the meaning of income. First, in section 2(24) says the income includes, between other, profits and gains, dividend, voluntary contributions received, the legal disposition still remits to incomes addressed in other sections, such as 28th. Section 2(45) establishes the concept of "total income", considering it as " the total amount of income referred to in section 5". In section 5, determines it includes all the income, regardless the source, it means the inclusion of: "(a) is received or is deemed to be received in India in such year by or on behalf of such person ; or (b) accrues or arises or is deemed to accrue or arise to him in India during such year ; or (c) accrues or arises to him outside India during such year". All Chapter III of ITA exposes to the incomes which do not form part of the total income. Chapter IV clarifies the determination of business' income, and the 28th section exposes the income taxation of the profits and gains of business or profession. The following section clarifies the rule to compute the income referred in the previous section is in sections 30 to 43D. The segments 30 until 43D determine guidelines for expenses deduction in the profit's estimation. The income rule allows the deduction of, for example, the amount paid the current repairs of machinery, plant and furniture[6]; the tangible assets depreciation[7]; expenditure on scientific research[8]; or other deductions[9], as well as the amounts not deductible[10]. It means Indian legislator uses the analytical method in taxable base's determination of corporate income taxation (Pascual and Zamora, 1998). It establishes tax regulation that normalises all the positive and negative components of the tax base (Martín Queralt and Moreno, 1998). It is a complete and exhaustive regulation of all elements and circumstances that determine income (income, expenses, the temporal imputation, valuation of the elements, extraordinary operation) through rules recognised by the Tax Law (Taboada, 1982). This method was used in countries such as Spain until 1995 when the current corporate income tax law came into force.

[6] Section 31.
[7] Section 32.
[8] Section 35.
[9] Section 36.
[10] Section 40.

Until that date, the law provided for complete independence between the accounting rules and corporate income taxation ones (Aldeia, 2017). Therefore, it promoted a doubling of accounting and tax rules (Moreno, 1997), that is what happens at this moment in Indian Tax Jurisdiction. Also, the law settles[11] The assessment year represents twelve months; it starts on the 1st day of April every year and finishes at the 31st of March next year. According to section 4 - Charge of income-tax is due to tax over the chargeable event occurred during the assessment year since predicted in ITA law disposition. Indian legislation assumes a proportional rate and being in a corporate tax dimension. There are no personalisation elements, that is, elements that allow adjustment to the personal conditions that occur in the taxpayer (Martínez, 2003). The corporate income rate in India differentiate the company's dimensions, taking into consideration if whether it is a small, medium or large business[12]. The large entities are subject to higher taxation, opposing the smaller ones. The first ones assume an ITA tax rate of 30%.

## 4. CONCLUSION

This article seeks to understand how corporate income taxation in India occurs and if corporate tax constitutes a competitive factor for Indian companies. The results show an inverse relationship between the number of Indian corporate taxpayer and the total contribution's amount to income tax revenue. Corporations represent 3% of the total taxpayers' number and contribute 57% of income tax revenues in the assessment year of 201-18. The fact that the income of individuals is low may justify this situation. However, it is undeniable the companies' duty to sustaining public burdens contribution. Moreover, there is a negative relationship between the taxation level and economic growth; it assumes that jurisdictions that show higher economic growth presents a minor proportion of taxes on corporate income and profit. Looking to YA 2017-18 data (table 1 and 2), it is possible to conclude that each corporate taxpayer (companies and firm) supports, on average, an annual tax burden of 0,26512 crores. The individual taxpayer pays 0,00597 crores by assessment year of income tax, on average as well. It means that who, effectively, supports Indian income tax is the corporations in opposition to individuals, even though, in general, the total income tax burden is lower, to companies and individuals, compared to other countries. The tax system simplicity constitutes a relevant characteristic to countries economic development because it is attractive to taxpayers, they feel more self-assurance on correct law's application, and it represents evident benefits to both sides, taxpayers and tax authority. Indian ITA is an old law, it is close to 60 years old, and although over the time it had amendments, it is a law that has endured in the time. It means predictability in business' operations. Investors feel the security to take economic decisions. The Constitution of India also has ancient writing. It maintains the original predictions about the regulation of the tax system. This predictability characteristic in both laws, both the ITA and the Constitution, give international investors favourable legal certainty for conducting business and raising foreign capital. It is not always the case in European countries, which, despite low CIT rates, are not competitive due to the complexity of the tax system. The Indian legislator, a long time ago, was able to enact and maintain a lasting law that taxes income earned in India, it constitutes a very favourable point for India's business development. However, it presents some differences in legal dispositions. This law regulates the taxation of singular and legal persons' income it makes a long norm; also, the assessment year is not the civil one, but it starts and finish in different years; furthermore, it predicts tax guideline that regulates the tax bases' incomes and expenses, it means that there a duplication of rules in accounting and tax dimensions. It can be to point some similarities to the current corporate law of Europeans countries, such as Portugal

[11] Section 2(9) of Indian ITA.

[12] http://taxsummaries.pwc.com/ID/India-Corporate-Taxes-on-corporate-income and https://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-corporate-tax-rates.pdf Consulted on September 12, 2019

and Spain, is the case of the income taxation of resident and non-resident entities and the implicitly of the territory tax principle, and the use of a proportional tax rate over the companies' profits. In Supreme law ambit, it determines, explicitly, the principle of legality as the base of the tax system, due to the requirement of tax imposition to the authority of law. This research allows to better understand the Indian tax system's role in the country's economic growth, mainly in corporate domains. It permits to identifies positive and negative corporate income tax law's characteristics that can promote the economic prosperity of companies in that geographic area. It could be relevant to replicate this study to other countries with similar economic growth behaviour, such as China, India's neighbour. As study's limitation, it is relevant to mention the difficult to interpret the ITA, taking into consideration its writing age, and the fact that that research only analyses the Income-Tax Act of 1961 and the Constitution of India, but it could be interesting to look other legal rules of the Indian Tax System.

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