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# Economy

## # Double Taxation

Direct tax such as income tax is imposed either on the basis of residential status of tax payer or on the basis of place of earning.

The Problem of double taxation arises when a person (individual or a firm) ~~may be residence of~~ resides in one country but earns from some other country. Many individuals and companies have multiple sources of income earned from different countries. for eg:- An Indian resident can earn interest from singapore and rent from US, profit from Mauritius and so on.

In principle, incomes from abroad must be taxed either in India or outside. But because of different rules of taxation there is a possibility the tax payer is asked to pay tax in both the countries. This happens when one country is following the residence rule while the other country is following the place of earning rule.

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Citizen Vs Resident

NRI - Non-Resi but Indian Citizen

# Tax Treaty

DTAA / DTAT (Double Taxation Avoidance Agreement)

To solve the problem of double taxation governments of different countries started siging agreement called double taxation avoidance agreements which provides relief to the tax payers in different ways. A common method is tax credit, which means deduction ~~dedection~~ of tax from the tax liablity in India. to the extent of taxes already paid abroad.

eg: Income (from US) $10 million

→ Tax paid in US say 20% $2 million

→ Tax in India @ 30% $3m

Less - $2 m = $1 m

Total 30% ← 20%, ← 10%

| | (Tax Casecading) TC | DT (Double Taxation) |
|---|---|---|
| Relates to | Indirect Tax on Goods & Services | Direct Tax on foreign incomes |
| Stages | Multiple | Two |
| | NAT | DTAA |

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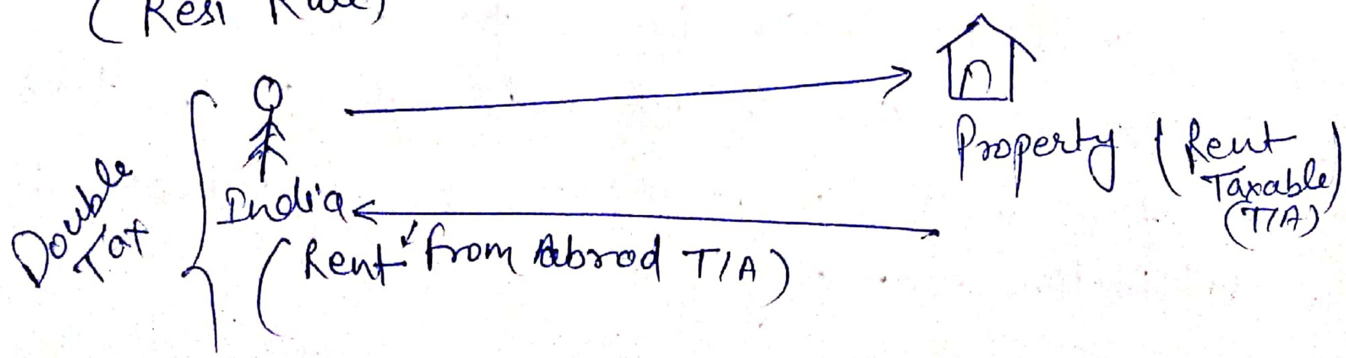
# Double non-taxation

Some multinational entities misuse the provisions of tax treaties (DTAA or DTAT) to avoid paying taxes in both the countries that is to say the country of resident and the country of earning income.

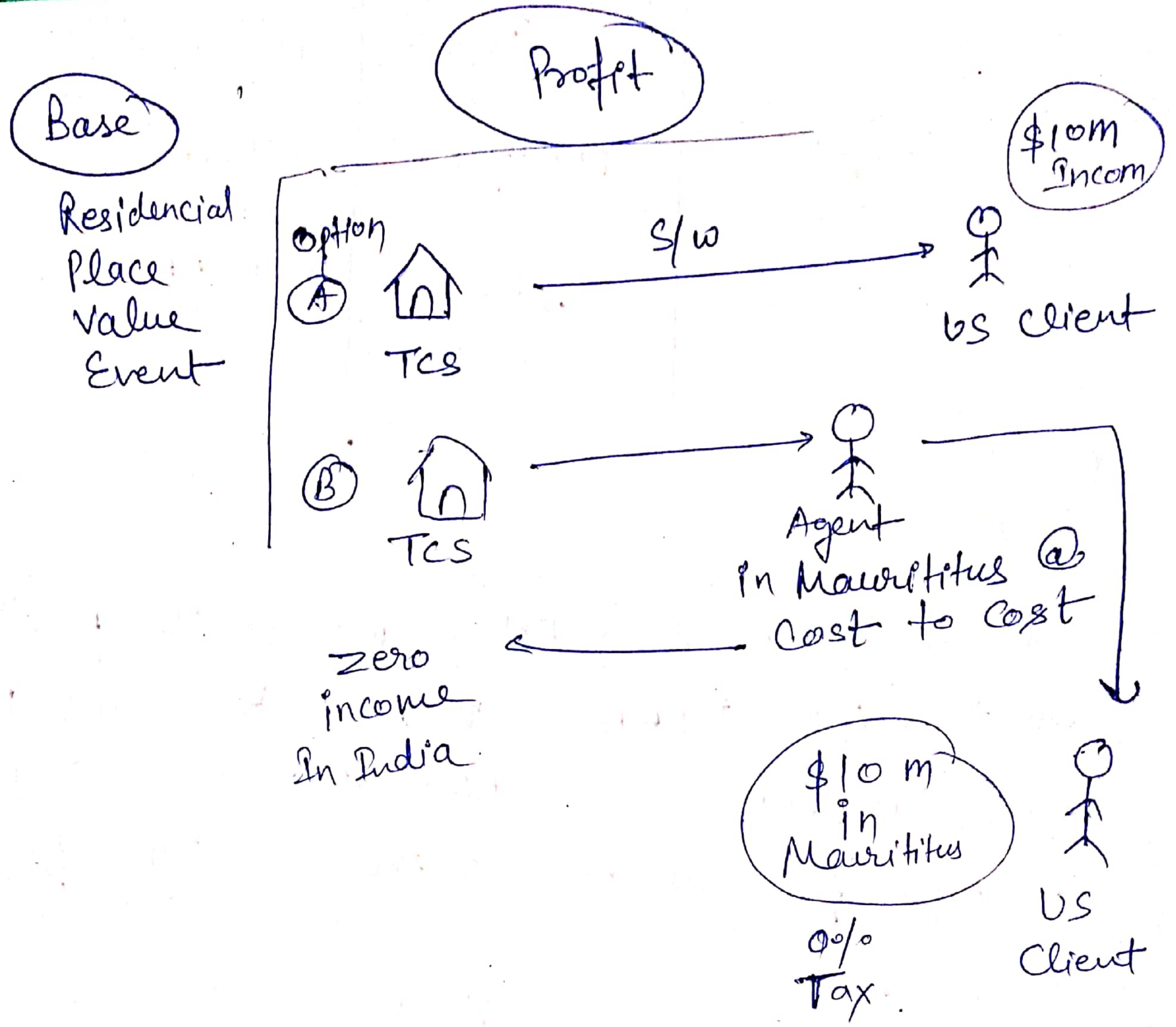
Such misuse is possible because of the loopholes provided in the tax laws of the different countries or in their tax treaties.

This problem is known double non-taxation.

eg. India (Resi Rule) Other country (Place Rule)



# BEPS (Base Erosion & Profit Shifting)



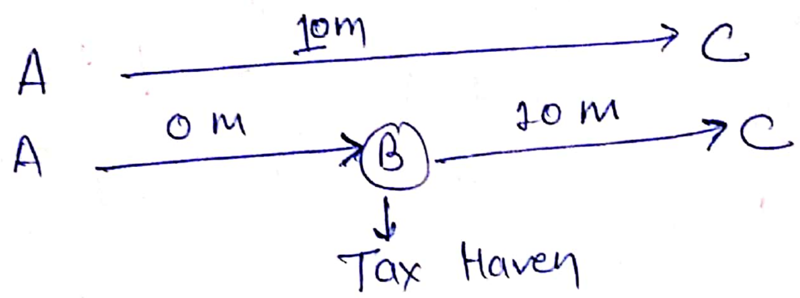

Abuse or misuse of tax treaties (treaty shoping) is a global issue because several multinational entities follow this for tax avoidance. Hence the Organisation for economic cooperation and development (OECD) has shown concern in this respect which is reflected in their BEPS, action plan 6. It prevents grant of treaty Benefits under inappropriate circumstances to the multinational entity.

It clearly states that tax treaty should not be used for double non- taxation and it should be ensure that profits are taxed in that country where economic activities generating such profit takes place and where value is created. This is possible if multinational entities are asked to present Country by country repost of their total profits so that it is insured that they are paying tax in the countries according to their economic activities. They must not be allowed to avoid tax payment in most of the country by misusing treaty.

India had a tax treaty with Mauritius which allowed tax benefits to Mauritius investors on their capital gains. Several Indian investors opened companies in Mauritius an invested through them in Indian markets to enjoy a tax benefit. This loopwhole existed for long time which is now closed after the amendment in 2016.

Transfer pricing agreements were common method used by the multinational companies to shift their profit from a high tax country to a low tax country. Transfer pricing is pricing of transaction among the related companies at hypo-thetical prices. which are much below the market prices and used for profit shifting.

for eg. Sell of services from an Indian company to some American client can be routed through any low tax country ~~like~~ called tax haven for eg.




# Tax Base

The proportion of people, firms, incomes, goods services, events or other factors which are subject to taxation of any kind.

To increase the tax revenue from both direct and indirect sources government tries to expand the tax base by including more and more factors under taxation. Still in India we have a narrow tax base for the direct taxes. It is obvious from the data of number of individuals and companies were filing their income tax statement every year. The data provided by the income tax department for the financial year 2017-18 shows that less than 6 Crore returns were filed Pan India of which 5.5 Crore relate to individual and 8.4 lakhs relate to companies.

$$\text{Tax Base for Income Tax} = \left(\frac{\text{Tax Payers}}{\text{Population}}\right)$$

$$\underline{\text{Returns}} = \left(\frac{5.5\ \text{Cr}}{137\ \text{Cr}}\right) = 4\%$$

The Income tax Base should also include those persons whose Income tax is paid or collected at sources or otherwise. But the Income tax return is not filed. That number must be around 2 crore.

$$\text{Others} = \left(\frac{2}{137}\right) = 1.5\%.$$

Making other 1.5% approximately. But because tax rate high in India for the Income tax. Hence Income tax collection remains between 45-50% of the total collection.

On the otherside tax base is broader of GST. Since it is collected from most of the costumers of Goods & Services.

According to Budget 2020 around 18% of the Total revenue is expected from GST. while 11% from the other Indirect taxes as compare to Income tax collection to the extent of 35%.

The recent measures taken by government including demonatization and digitalisation have increased the tax base for Income tax. substantialy because in 2013-14, Only 3.74 crore Individuals filed their return. Similarly after rolling out GST there was 50% expension in the tax base of the Indirect tax payers from around 70 lakhs firms. to 1 Crore 4 Lakh firms.

$$\boxed{\text{Tax to GDP Ratio} = \frac{\text{Total Tax Collection}}{\text{Total GDP}}}$$

eg → $= \frac{20t₹}{200t₹} = 10\%$