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AN OVERVIEW OF DIRECT TAXES CODE BILL

AUTHORED BY- AYUSH PATIDAR & SNEHA SHARMA

I. INTRODUCTION

1. India's direct tax system needed reform and simplification, hence the Direct Tax Code (DTC) Bill, 2010, was an important legislative initiative. The Direct Tax Code, a single, comprehensive piece of legislation, was intended to replace and modernise the current tax laws, mainly the Income Tax Act of 1961 and the Wealth-tax Act of 1957.¹
2. The Standing Committee on Finance² has agreed the Chairman permission to present this 49th Report on "the Direct Taxes Code Bill, 2010." On September 9, 2010, the Speaker of the Lok Sabha, acting in accordance with Rule 331E of the Rules of Procedure and Conduct of Business in the Lok Sabha, referred the Direct Taxes Code Bill, 2010, which had been tabled in the Lok Sabha on August 30th, to the Committee for review and a report thereon.
3. The Committee overheard oral testimony from the Ministry of Finance's (Department of Revenue) official during its meetings on November 18, 2010, and November 11, 2011. The Committee received the opinions of the Confederation of Indian Industries (CII) and Institute of Chartered Accountants of India (ICAI) representatives at their conference on January 19, 2011, in which it was held. Representatives from NASSCOM, the Export Promotion Council for EOUs and SEZs, Earnest & Young Private Limited, KPMG, the Coalition of International Taxation in India, and the Cellular Operators Association of India shared their perspectives with the Committee during the meeting on October 17, 2011.³
4. Several stakeholders' thoughts were also heard by the Committee during the study. These stakeholders comprised the Bombay Chambers of Commerce, Bombay chartered Accountants Society, General Insurance Council and Life Insurance Council, Indian Merchant's Chamber, Madras Chambers of Commerce and Industry, Income Tax Appellate Tribunal Bar Association, Mumbai, Saifee Hospital Trust, National Sea Farers

¹ Lok Sabha, F. (2012). STANDING COMMITTEE ON FINANCE (2011-12) THE DIRECT TAXES CODE BILL, 2010 FORTY-NINTH REPORT LOK SABHA SECRETARIAT NEW DELHI (Saka) 2 FORTY-NINTH REPORT STANDING COMMITTEE ON FINANCE (2011-2012) (FIFTEENTH LOK SABHA) THE DIRECT TAXES CODE BILL.

² Supra note 1

³ Supra Note 1

Association, Container Shipping Lines Associations, All India Federation of Tax Practitioners, e When the study group visited Srinagar on the 15th and 16th of June 2011, they also spoke with the Income Tax Department about a few tax administration-related issues.⁴

5. The Committee examined the draft Report on "the Direct Taxes Code Bill, 2010" at its meetings on February 10, February 17, and February 24, 2012, and adopted it at its meeting on March 2, 2012. The Committee would like to thank the Ministry of Finance (Department of Revenue) staff members involved with the Bill for their cooperation as well as all the groups and experts for their insightful comments on the Bill.⁵

➤ **Need for complete review of the prevailing Income Tax and Wealth tax Acts⁶**

1. The Committee desired to know whether it was compulsory to conduct a thorough review of the contemporary Income Tax and Wealth Tax Acts. The Ministry of Finance (Department of Revenue) responded in writing. stated as follows:
2. The Income-tax Act of 1961 has undergone a number of modifications in the fifty years after its passage. It has endured significant revisions, not by amendment, less than thirty-four times. Further Acts to the Amendments carried out by means of the yearly Finance Acts. These variations were required by policy adjustments brought about by the fluctuating nature of the economy, the sophistication of commerce, the rise in international trade fetched about by globalisation, the expansion of information technology, efforts to reduce tax avoidance, and the necessity to make the law clearer in light of recent court rulings. The Income Tax Act's central structure has been overburdened and its language has become complicated as a result of all these revisions. The Act is particularly challenging for the average tax payer to understand due to the numerous revisions. The Wealth-tax Act of 1957 has also undergone changes.
3. Therefore, the government made the decision to update, combine, and simplify the wording and framework of the direct tax legislation. In August 2009, a draught of the Direct Taxes Code and a Discussion Paper were made available for public feedback. The Income-tax Act of 1961 and the Wealth-tax Act of 1957 were to be replaced by the Direct Taxes Code, a single Act.

⁴ Standing Committee, Supra note 1

⁵ Supra Note 1

⁶ Dr. Justice A.R. Lakshmanan, D.D. Basu, *Shorter Constitution of India*, 1683 (14th Ed. 2009).

➤ **Objective**

The core objective of direct tax code bill is:⁷

- to rationalize and accumulate all central government direct tax laws.
- to advance the effectiveness and efficiency of the tax system.
- transporting the combined direct tax law, which comprises the income tax, the dividend distribution tax, the fringe benefit tax, and the wealth tax.
- to achieve horizontal equity among various taxpayer classes in accordance with best global practises.
- Tax regulations must be clear, reliable, and strong if they are to rise acquiescence even further.
- to progressively reduce the amount of tax breaks and deductions in order to increase and delve deeper into the tax base.

I. STATEMENT OF PROBLEM(ISSUES)⁸

Formerly going over the several concerns carried up by the Committee and their detailed observations/recommendations clause-by-clause (Part-II), it may be supportive to briefly discover the Committee's analysis of certain larger issues:

1. To streamline tax law and broaden the revenue base, a draught of the Direct Taxes Code, 2009 was released for public comment. Some of the provisions of that Draught Code are changed by the Bill.⁹
2. Tax breaks for individuals have been reserved, but most business exemptions have been eliminated. Individual tax rates have been reduced. Corporate taxes will subsidize additional to the government's revenue than they did in the past.
3. In two ways, the Bill might make compliance more difficult. The General Anti Avoidance Rules' application circumstances are not specified in any guidelines. The Bill also orders that the tax liability for income from numerous business units must be resolute separately.

⁷ Dr. Justice A.R. Lakshmanan, D.D. Basu, *Shorter Constitution of India*, 1683 (14th Ed. 2009).

⁸ Lok Sabha, F. (2012). STANDING COMMITTEE ON FINANCE (2011-12) THE DIRECT TAXES CODE BILL, 2010 FORTY-NINTH REPORT LOK SABHA SECRETARIAT NEW DELHI (Saka) 2 FORTY-NINTH REPORT STANDING COMMITTEE ON FINANCE (2011-2012) (FIFTEENTH LOK SABHA) THE DIRECT TAXES CODE BILL.

⁹ Supra note 7.

4. The Dividend Distribution Tax and the Security Transaction Tax are still involved in the Bill. These taxes disturb the idea of progressive taxation of people since they are levied at a fixed rate irrespective of the amount of income or profit.
5. The Bill objects to tax foreign businesses whose "effective management" location at any given time of the year is in India. What would institute effective administration of a foreign corporation in India is uncertain.

➤ **The Committee's study of the subsequent broad issues may be fleetingly discussed:**

1. How significantly the 1961 Income Tax Act has been abridged?-

The Committee was concerned in learning how much the DTC Bill will abridge the current Income Tax Act of 1961. The Ministry responded in writing as follows: "The Statement of Objects and Reasons as given by the Finance Minister on August 27, 2010 elucidates that the 1961 Income Tax Act was revised at least thirty-four times, leading to "complexity in tax laws" and the incapability of the average tax payer to comprehend it. Thus, the goalmouth of the new tax code is to amend, syndicate, and simplify the language and framework of Direct Tax Laws.

When asked what fundamental developments the Direct Taxes Code has made to the previous Direct Tax Laws to make them clearer and easier to comprehend, the Ministry responded in writing as follows.

- a) By using direct, active speech, communicating just one idea through a single subsection, and rearrange the laws into a logical framework, it streamlines the language of the legislation.
- b) 9 provisions (sections 115A to 115BBB) of the Income Tax Act of 1961 currently discourse the tax rates for non-residents on particular incomes. These are now characterized as special source incomes, and Part III of the First Schedule of the DTC details the tax rate.
- c) It enhances the taxes rules for cross-border transactions. It has become vital to establish a robust framework for the taxation of cross-border trade and global capital in the context of a globalized economy. These are reflected in the new regulations.

2. Concerning resident corporations- the challenge raised is that business income must be calculated distinctly for each distinct and separate business, irrespective of whether each such business receives tax benefits, and that given how distinct and separate

businesses are well-defined, a important amount of additional time, effort, and expense is likely to be incurred.

- 3. Taxation of non-residents** - It should be noted that taxation of non-residents is a complex topic as a outcome of globalization, the uncomplicatedness of capital transfers between nations, the simplicity of changing residence by establishing a company in a foreign jurisdiction, the rise in transactions between related entities within multinational corporations, etc. Sovereign governments must discourse these complications not only in the area of taxation but also in the zones of business regulation, competition regulation, capital market regulation, and banking and monetary regulation.

Other nations are also dealing with these multifaceted issues, and India's provisions concerning the location of effective management, the indirect transfer of Indian assets outside of India, and CFC regulations are constant with those in place in other countries. Protecting one's tax base is crucial in a system with moderate tax rates. Indian efforts to shield its tax base and make sure that taxes owed to it are recorded and paid in India would be delayed by the absence of such procedures and rules.

II. LITERATURE REVIEW

- 1. A picture of the research paper**- This paper evolves around the Direct Tax Code (DTC) Bill, 2010, which was an important legislative initiative. The Direct Tax Code, a single, wide-ranging piece of legislation, was intended to substitute and modernise the current tax laws, mainly the Income Tax Act of 1961 and the Wealth-tax Act of 1957.

The Standing Committee on Finance has given the Chairman permission to present this 49th Report on "the Direct Taxes Code Bill, 2010." On September 9, 2010, the Speaker of the Lok Sabha, acting in accordance with Rule 331E of the Rules of Procedure and Conduct of Business in the Lok Sabha, referred the Direct Taxes Code Bill, 2010, which had been tabled in the Lok Sabha on August 30th, to the Committee for review and a report thereon.

Under this paper the reader will get the idea of key issues related to tax laws and the observations related to the same.

Reader would be able to analyse the tax bill by reading recommendations related to the introduction of the bill.

2. A summary of the research paper's main points-

<p>Legal Framework- further down this paper the author has conferred the Bill which comprises the following significant global best practices:</p> <ol style="list-style-type: none"> 1. Place of effective management will serve as the company's base of operations. 2. Advance Price Contracts 3. low-tax or uncooperative jurisdictions 4. Instead of a higher rate of taxation, international corporations will now be subject to the Branch Profit Tax.
<p>Key issues-</p> <ol style="list-style-type: none"> 1. simplification of Income Tax act 1961 2. Regarding resident corporations- 3. Taxation of non-residents
<p>Judicial Rulings- The case mentioned in the paper highlights the importance of maintain the separation of power and an independent judiciary when forming specialised tribunals</p>

3. **Gaps in research-** the research paper evolves around the important laws that were being amended by the bill. The research paper does not suggest any suggestion by authors and is clearly an overview of the bill.
4. **An evaluation of Research paper's contribution to the topic-** This paper will boost the knowledge of the readers as it explains the concept in an easy and comprehensive knowledge. All the references mentioned are authentic in nature and can be beneficial for the reader.

III. RESEARCH METHODOLOGY-

Qualitative Research- this research is made based on the observations made by the Standing Committee in *MINUTES OF THE TWELFTH SITTING OF THE STANDING COMMITTEE ON FINANCE (2011-12)* and through 49th Report of Ministry of Finance. This research is accurate because it is taken from primary sources. All the comments and observations made by the committee are taken as it is without any alterations.

The research is conducted from the official act as well as from books. The said sources were used and analysed and interpreted based on the facts.

The relevant laws mentioned in the paper are directly taken from the DIRECT TAXES CODE, 2010 (Bill No. 110 of 2010) and Ministry of Finance, Government of India, Report of the Taxation Enquiry Commission¹⁰.

All the information was processed from ministry of finance's website. The information was analysed and then distributed as per the headings.

The reason for relying on the primary sources was its reliability and authenticity.

IV. LEGAL FRAMEWORK

➤ Key International tax practices/provisions incorporated in the Code¹¹

1. Residence of company to be based on Place of effective management

Bestowing to the current tax code, a corporation is deemed to be a resident of India if it was incorporated there or if all of its management and control are situated there. However, if a corporation's "place of effective management" is in India, the code treats that firm as if it were incorporated in India.¹²

2. Provision for Controlled Foreign Companies (CFC) to offset adjournment of income repatriation¹³

It is also proposed to introduce Controlled Foreign Company provisions as an anti-avoidance measure, in accordance with generally accepted practices, so that passive income earned by a foreign company that is controlled directly or indirectly by a resident of India, and where such income is not distributed to shareholders resulting in tax deferral, shall be deemed to have been distributed. As a result, resident shareholders would be required to pay taxes in India on the dividend they received from the overseas firm.

3. Advance Pricing Agreements¹⁴

The DTC contains a clause that permits the Board to sign an Advance Pricing Agreement

¹⁰ Vol. III, (New Delhi, India, 1953-54), 181-330.

¹¹ THE DIRECT TAXES CODE, 2010. (n.d.).

¹² Ibid.

¹³ Ibid.

¹⁴ Ibid.

(APA) with any individual who will be handling an international transaction. The APA will outline how to calculate the arm's length pricing in connection to such an international transaction.

➤ **New Principles Introduced in DTC**

1. Tax rate under the code

All tax rates under the Code are proposed to be listed in the First through Fourth Schedule of the actual Code. If there are no plans to alter the tax rates, there is no longer a need for an annual finance bill. If there are any modifications to the rates, they will be implemented by suitable amendments to the Schedule that will be presented to Parliament as an Amendment Bill. Through amendment bills, other changes to the Code will also be made.

2. Financial year

The income generated in one year is taxed in the following year under the existing Income Tax Act of 1961. When income is earned, the year is referred to as the "previous year," and when it is taxed the next year, it is referred to as the "assessment year." Both compliance and administration have experienced misunderstanding as a result of the employment of the two expressions. The previous idea of an assessment year has been abandoned.

According to the Code, the 'financial year' will be the basis for all of the taxpayer's and the tax administration's rights and obligations.

3. Total income

To govern the taxpayer's "total income," the "total income from ordinary sources" and the "total income from special sources" will be joint.

4. Loses

The loss under the heading "Capital gains" must be kept isolated, and it cannot be offset in contradiction of income under other headings. Similarly, any losses incurred through trading in speculative securities and from maintaining and caring for horses for the purpose of horse racing will similarly be ring-fenced.

As an alternative of the current law's limitation of carry forward for only eight years, losses would be allowable to be carried forward indefinitely for set off against earnings in the subsequent fiscal years.

5. GAAR- (General Anti Avoidance Rule)

Tax evasion and avoidance both considerably impair the fulfilment of the public finance goal of equitable, efficient, and effective revenue collection. Sectors that offer more opportunities for tax evasion typically led to distortions in the way resources are allocated. The DTC has implemented a general anti-avoidance regulation that will function as a deterrent against such behaviours.

6. Arrangement of Income

In principle, all accruals and receipts in the arrangement of revenue must be categorised as either "special sources" or "ordinary sources."

Nothing can be deducted, and the gross amount is liable to tax, usually at a reduced rate. This is how presumptive taxation is used. Only the percentage of these "special source" incomes that is derived from India is subject to tax under the Code, hence they are primarily applicable to non-residents. The "ordinary sources" of income are determined by determining the net income after deducting permissible expenses from revenues and are applicable to both residents and non-residents conducting business through a permanent presence in India.

An "ordinary source's accruals or revenues will be further categorised under one of the following five heads:

Income from:

- A. Employment
- B. House property
- C. Business
- D. Residuary Source
- E. Capital Gains

V. JUDICIAL RULINGS

1. **The McDowell's Case rule**¹⁵ (henceforth referred to as "McDowell") has generated a great deal of debate in the field of tax governance. On the one hand, it might appear to have fundamentally altered tax planning and fiscal jurisprudence in India, but some

¹⁵ McDowell and Co. Ltd. v. CTO, (1985) 3 SCC 230 : AIR 1986 SC 649.

authors believe that this is untrue and that the Supreme Court's otherwise persuasive explanation of fiscal principles is only an aberration.¹⁶ The ambiguity surrounding the legal position on tax planning has been exacerbated by judicial pronouncements made subsequent to the McDowell case. This has led to radically different opinions about what should and should not be allowed when determining an assessee's tax liability through transactions. Consequently, it is argued that removing much of the surrounding gloss is essential to determining the precise impact of the judicial pronouncements in question. This will allow us to answer two questions: what the court actually did and what it intended to achieve.

2. **In Vodafone**¹⁷, the Bombay High Court determined the nature of the transaction for the narrow goal of deciding that the notice was not completely nonest²⁶. It did this on two reasons by upholding the show-cause notice given to the petitioners. First off, the deal involved the transfer of the subsidiary's underlying assets rather than just shares, which would have transferred the Cayman Islands entity's majority interest in its Indian subsidiary. Any profit made by the subsidiary would be subject to taxation in India as "capital gains" since it would be seen as the transferee's profit as well as the profit of the "shell company." Second, the Court determined that a simple transfer of the controlling interest implied a transfer of several valuable intangible assets, including the right to conduct business and run mobile phone operations in India, which transfer was taxable in India, even in the absence of "piercing the veil" and treating the subsidiary's assets as the subject of the transfer.

VI. KEY FINDINGS AND RECOMMENDATIONS

With regard to further direct tax reforms, it may be mentioned that tax experts have proposed a Direct Tax Code (DTC) to simplify the structure of India's direct tax laws into a single Act and replace the existing Income Tax Act, 1961. and other direct tax laws related to wealth tax and dividend tax. Direct tax laws are proposed in three strategies to expand the tax base.¹⁸

¹⁶ See NANI PALKHIVALA ET AL., *The Law and Practice of Income Tax* 66 (9th Edn., Dinesh Vyas Ed., 2004)(hereinafter "Palkhivala").

¹⁷ *Vodafone International Holdings v. Union of India*, 2008 SCC OnLine Bom 1152 : (2009) 311 ITR 46.

¹⁸ Rao, K. R. and Chakraborty, P. 2010. Goods and services tax in India : An Assessment of the Base, *Economic & Political Weekly*, XLV (1), January 2.

- (1) Minimize tax breaks and tax breaks that erode the tax base.
- (2) removing loopholes and anomalies in existing direct tax laws that facilitate tax avoidance;
And
- (3) Combating tax evasion.

1. Case Management: Amendments to Sections 147 and 148 of the I-T Act allow tax authorities to reopen assessment cases based on pre-defined criteria.¹⁹

- I-T personnel can examine the assessed books and records going back six years.
- These regulations are currently open to interpretation. 40% of the cases are because the assessed challenges the reasons given by the officer for reopening the case.
- Increased threshold limit for filing a claim: Now it is more than Rs 100,000. The predetermined criteria for selecting cases for review will also be tightened.
- Proper reasons must be supported to reopen the case.
- Assessment procedures should be faceless and citizens should have the option to explain tax issues to CBDT.

2. **Reducing the burden of tax compliance**²⁰: tax compliance based on global trends and best practices. This is expected to increase transparency among taxpayers and broaden the tax base.

- Use of artificial intelligence (AI) in tax compliance and administrative processes.
- Cooperative compliance proposal in direct taxes department. It integrates data from banks, financial institutions and the Goods and Services Tax (GST) network to ensure a wide range of taxable income.

3. **Personal income tax: Tax rates are set between 5 and 20 percent.**²¹

Currently, the personal income tax structure is divided into three categories based on age. People under 60 years old, people over 60 years old but under 80 years old, and the third category are people over 80 years old.

- There are four berths in the first category where income up to Rs 2.5 lakh is exempt from tax. A tax rate of 5% applies to incomes between Rs 2.5 million and Rs 5 million, a tax

¹⁹ Rao, M., Rao, G. and Rao, K. R. 2009. Direct taxes code : Need for greater reflection, Economic & Political Weekly, XLIV(37), September

²⁰ Shetty, S.L. 2010. More tax concessions for more inequality, Economic & Political Weekly, 2010 XLV (11), March 1

²¹ Shetty, S.L. 2010. More tax concessions for more inequality, Economic & Political Weekly, 2010 XLV (11), March 1

rate of 20% applies to incomes between Rs 5 million and Rs 1 million and a tax rate of 30% applies to incomes above Rs 1 million. The second tier has a base slab of Rs 300,000 and the third tier has a 'zero' interest rate for income up to Rs 500,000.

4. Corporate tax will be 25%²²

- The government plans to reduce the corporate tax rate to 25% in a phased manner for all companies, including large companies with an annual turnover of more than Rs 400 crore.
- Over the past five years, the government has gradually reduced the tax rate from 30% to 25% for 99.3% of businesses.
- However, the 0.7% of large companies that do not take advantage of this benefit account for almost 80% of the total corporate tax collection and are subject to up to 30%.
- The proposed reduction in corporate income tax will apply to both large local and foreign companies operating in India without a subsidiary and taxed at 40%.

The direct tax law is expected to lead to benefits such as increased tax-to-GDP ratio, increased GDP growth, improved fairness, lower administrative burden and lower compliance costs. In connection with the implementation of the Act on Direct Taxes, it can be pointed out that the proposed tax reform has yet to be implemented. Although the Direct Tax Bill was introduced in Parliament in 2010 and a revised version of the bill was issued by the government in 2014, the bill could not be passed in Parliament due to the fall of the then government. In 2017, the government established an expert commission to draft a new code of direct taxes. Although the committee's report was submitted to the Finance Minister, Ms. Nirmala Sitaraman on 19 August 2019, the report has not yet been made public.²³

VII. CONCLUSION

The Direct Tax Code (DTC) Bill of 2010 represented a significant step towards modernizing India's direct tax system. The objective of the proposed Direct Taxes Code (2010) is to create a single piece of legislation known as the Direct Taxes Code (DTC), which would substitute both the Income Tax Act of 1961 and the Wealth Tax Act of 1957. The Direct Taxes Code was introduced with the claimed goals of streamlining the tax system, reducing litigation, expanding the revenue base, and doing away with exemptions.

²² Rao, M., Rao, G. and Rao, K. R. 2009. Direct taxes code : Need for greater reflection, Economic & Political Weekly, XLIV(37), September.

²³ The Indian Journal of Commerce Vol. 64, No. 2, April-June 2011.

Despite having objectives to reduce tax evasion and simplify India's direct tax system. The law has enormous potential to streamline taxation, lower tax evasion, and comply with global best practises. However, it encountered difficulties, complexity, and amendments throughout the legislative process. There have been numerous adjustments and discussions as a result of stakeholder concerns, the complexity of the additional laws, and shifting political objectives. The DTC bill of 2010 ran across a number of obstacles that hindered its advancement. These difficulties can be explained as follows:

- **Stakeholder Concerns:** Businesses, tax professionals, and the general public were among the stakeholders who engaged in extensive discussion and debate over the proposed legislation. The projected elimination of tax deductions and exemptions was one of the main points of dispute. Many people claimed that these exclusions were necessary for promoting investment and economic expansion.
- **Complexity of the Tax System:** The bill offered new ideas and regulations while also attempting to simplify the tax system. Some of these new rules, such as the adoption of General Anti-Avoidance Rules (GAAR), have drawn criticism since they are thought to complicate the tax code and increase the likelihood of disagreements between taxpayers and tax authorities.
- **Economic Effects Concerns** about the DTC bill's possible effect on economic growth have been voiced by some experts and industry executives. They were concerned that eliminating such tax breaks may deter investment and weaken India's competitiveness.
- **Political changes include:** During the course of the bill's passage through the parliamentary process, India's government underwent changes and its political priorities shifted. As a result, the government's strategy for tax reform changed, which hampered the bill's advancement.

The DTC bill sought to harmonise India's tax system with global best practises by modernising and streamlining it. However, because there are so many competing interests, reaching agreement on such measures frequently takes time.