

A STUDY OF TAX PLANNING AMONG INDIAN NATIONALS

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INTRODUCTION TO TAX PLANNING:

Since the inception and introduction of IT Act over the last 80 years, it has been in daily argument that there is a big fight between the taxpayers and tax collectors that is govt. It is because of the fact that the taxpayers continuously trying to reduce their tax liability because they cannot fully avoid the tax liability and the govt is always trying to correct the mistakes in IT Act or trying to plug in the loop holes from the IT Act so that the IT liability of taxpayers can be increased.

So from the above explanation “Tax Planning” can be defined as “An arrangement an Individual or any persons [defined by IT act in 2 (31)] made by them for the purpose of reducing their IT liability to the minimum by taking complete benefits of all deduction, exemptions, allowances and rebates within the legal framework of IT Act 1961 is tax planning”.

Let’s understand the tax planning with the help of an e.g. Let Mr. A is an Individual for A.Y. 2018-19, his GTI is Rs. 3,50,000. Therefore, his tax liability is Rs. 5,000. If Mr. A had invested Rs. 50,000 in PPF the tax liability will be Rs. 2,500.

So from the above his tax liability from 5,000 to 2,500 by using deduction u/s 80C which is under legal framework of IT Act, therefore it is tax planning.

However, tax planning is different from tax avoidance. Tax planning involves using all the instruments specified in the IT act to minimize the tax liability where as tax avoidance is using the loopholes or mistakes of IT Act to reduce the tax liability. And therefore, tax avoidance and tax planning both are legal ways to reduce the tax liability. Tax avoidance can be better understand by an e.g.

If a sum of money is gifted by a husband to his wife, income generated from that gifted money is taxable in the hands of husband under specific provisions contained u/s 64 (1). The clubbing of Income under this section is not applicable if the gift given by the same person out of the funds of his HUF in capacity as Karta of the family. Therefore if the gift is given by

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the Karta of the family to his wife, the clubbing provisions u/s 64 (1) can be avoided and ultimately the tax liability will also be reduced.

Therefore, from the above e.g. it is clear that the tax liability will be reduced by taking the help of loopholes or mistakes in the IT act within the legal framework. Whenever IT liability is reduced by taking help of loopholes in IT laws is tax avoidance.

Tax planning is very different from Tax evasion because the tax planning reduces the tax liability by following the rules and procedures of IT act which means doing everything legally. However tax evasion can be defined as all the methods and means by which tax liability is reduced illegally is tax evasion. Any assessee if found guilty of tax evasion can be punished under the laws. Tax evasion involves presenting false statements knowingly, submitting false and misleading documents, hiding, facts and figures, not maintaining proper books of accounts of income earned (if required under the IT laws) omission of material facts on assessment. All the methods and procedures are required by the IT act to be complied but the assessee who does not follow all these methods and procedures and tries to minimize tax liability before complying with the said rules, methods and procedures by making false statements, would be called as tax evader. For the purpose of IT payment evasion means "To illegally try to avoid paying taxes". Tax planning can be understood better with an e.g.. Section 80 IB of IT Act provides the deduction to the Profits and Gains from business if an industrial undertaking is setup in an industrially backward area.

Let TCS Ltd has factory in M.P. near Rajasthan border. Within the factory premises 4000 square meter piece of land is free and unutilized. The company had decided to setup a new unit to manufacture and sell computer components. If this manufacturing unit is setup in the prevailing factory campus, deduction u/s 80IB is not available but rent cost can be saved. However, if the new unit in setup in J&K, the company can claim deduction u/s 80IB. But they have to incur all the preliminary and rent expenses. So to get the benefit of deduction u/s 80 IB, the company must have to start the new unit in a village near J&K. Now the company has two options. One to avail benefit of deduction or one to avail the benefit to save preliminary and rent expenses but to avail benefit u/s 80 IB of IT Act the new setup must have to be situated near J&K. But if the process of manufacturing actually takes place in M.P. near R.J. Border. But to get the benefit of deduction u/s 80 IB, the company takes a factory building on rent in village in J&K and only on paper it is presented that the new manufacturing unit is situated in a village near J&K. Therefore, the company wants to reduce the tax liability by presenting false statements about the location of new manufacturing process, it is known as tax evasion.

Tax planning can be understand by a practical e.g. of a salaried employee. While framing the salary structure of an employee, employer has to keep in mind tax planning. Tax liability of an employee can be reduce if salary is divided into different allowances and perquisites. The

maximum utilization of allowances and perquisites depend upon employee's individual requirement that can reduce the tax liability of employee.

E.g. Mr. M has been offered an employment on monthly salary of Rs. 40,000 per month. If Rs. 40,000 is received by Mr. M as salary, his tax liability will be as follow.

Option I

| Particulars | Rs |
|--------------------------|----------|
| Salary (Rs. 40,000 x 12) | 4,80,000 |
| Net Income | 4,80,000 |

Calculation of tax liability:

| Particulars | Calculation | Rs. |
|----------------------------|---------------|---------------|
| Upto 2,50,000 | Nil | 0 |
| 2,50,000 to 4,80,000 | 2,30,000 x 5% | 11,500 |
| Total tax liability | | 11,500 |

Net home take of Mr. M = 4,80,000 – 11,500 = 4,68,500

Alternatively, Mr. M can take same salary in different forms of allowances and perquisites. While framing salary structure one has to ensure that expenditure incurred by employer should also be allowed as deduction for his return and allowances and perquisites, are not taxable or taxable at lower rate in hands of employee which means win-win situation for both the parties.

Option II

| Particulars | Expenditure incurred by employer | Amt taxable in hands of Employee |
|---|----------------------------------|----------------------------------|
| Basic Salary (18,000 x 12) | 2,16,000 | 2,16,000 |
| Employer's contribution towards recognized PF | 21,600 | - |
| Transport allowance | 9,600 | - |
| Education allowance for two children (Rs. 100 x 12 x 2) | 2,400 | - |
| Academic research allowance | 24,000 | - |
| Uniform allowance | 30,000 | - |
| Rent free accommodation | 72,000 | 72,000 |
| Amount spent by employer on medical treatment of employee in govt hospital. | 56,400 | - |

| | | |
|---|-----------------|-----------------|
| Free car for personal use of Mr. M but not for travel between office and residence. | 36,000 | - |
| LTC | 12,000 | - |
| Total Expenditure/ Gross total income | 4,80,000 | 2,88,000 |
| Less: Deduction u/s 80C (Being employees contribution towards provident fund) | | 21,600 |
| NTI | | 2,66,400 |

Now, calculation of tax liability:

| Particulars | Calculation | Rs. |
|----------------------------|---------------|------------|
| Upto 2,50,000 | Nil | 0 |
| 2,50,000 to 2,66,400 | 1,64,000 x 5% | 820 |
| Total tax liability | | 820 |

Net home take of Mr. M = 4,80,000 – 820 = 4,79,180

So from option I and option II it is clear that option II it is clear that option II is more suitable for Mr. M because it reduces the tax liability from 11,500 to 820 and also increases the net home take of Mr. M from 4,68,500 to 4,79,180 and it is suitable for the employer also because for all the expenses employer incur deduction is available for the employer. Therefore, it is proved that tax planning creates win-win situation for both the parties and tax planning give benefit to both employer and employee. Apart from this tax planning can also be done in the following ways.

1. Tax planning for Indians going to abroad:

If a person wants to go out of India for professional or employment the best planning is to plan an adjust the date of going to abroad in such a way that he becomes NRI, according to section 6 of IT act in very first year. He should also try to see that he becomes NRI in the second year too by spending less than 182 days in the second year in India. Once he becomes NRI for two consecutive year, for the next eight years he status even though he may continuously stay in India, would be a person or assessee R & NOR in India. This would give him benefit of exemption from taxes in respect of incomes earned from abroad.

2. Tax planning for Indian Citizens coming to India from abroad:

U/s 10 (5) of IT act Indian citizens employed in abroad are exempt from taxation of travel concessions subject to certain conditions specified in rule 2 (b) which definitely allows such concession but only once in a period of four years to employee himself and his family too.

The family for this purpose of leave travel concession 10 (5) does not only includes his wife and children but also his parents, brothers and sisters who are mainly dependent on him.

3. DTAA (Double Tax Avoidance Agreement):

Apart from this tax planning can also be done keeping in mind DTAA. Where the assessee of Indian origin who wants to go out of India for employment will make sure to choose such country which has DTAA agreement with India. Therefore, if the DTAA agreement exists he has to pay tax on income only in one country. Because if that country does not have DTAA with India then the assessee has to pay taxes in both the countries. There are certain provision due to which the assessee can decrease or reduce some amount of tax in India according to section 90 and 91 of IT Act but cannot avoid fully the payment of tax if the DTAA does not exist. However, if the assessee chooses a country which has no IT law like Dubai then also he has to pay tax only in one country that is India if he becomes resident in India in the P.Y. and no taxes to be paid in Dubai because IT does not exist in Dubai. However, if he becomes NRI in India in the P.Y. then he does not have to pay any tax at all in any country.

4. Findings

- i. Mostly People prefers to invest in Gold.
- ii. Growth in money is the reason for savings and investment.
- iii. The reason for not doing saving and investment is that they do not have enough money.
- iv. Most respondents expect returns from their investments in 2 to 4 years.
- iv. Respondents are not satisfied with the lock in period provided by the companies for investments.
- v. Most of the respondents feel that their investments are Liquid. vii. Respondents save 6 to 10 % of their income.
- vi. Respondents do not hire tax consultants to handle their tax matters.
- vii. Respondents feel that they hire tax consultants mainly for the purpose of filing of ITR.
- viii. Tax consultant advice respondents about ways for reducing tax liability.
- ix. Respondents are not satisfied by the fees charged by tax consultants.
- x. Most of the respondents are aware of the Section 10(33) exemption. (Dividend from Indian companies, Income from UTI and Mutual Funds).
- xi. Most of the respondents are aware of the Section 16 (ii) deduction. (Professional Tax).
- xii. Respondents feels that tax planning is concerned with tax saving.
- xiii. Respondents feel that demonetization affects tax planning.
- xiv. Respondents feel that digital economy is the benefit of demonetization.

xv. Respondents feel that more electronic system is the aftermath of demonetization.

5. Suggestions to the IT Act:

i. In section 16 (ii) of IT act 1961 that is entertainment allowance Deduction. Why it is only given to govt employees and not to private employees. This is a total partiality and this must be corrected in IT law.

ii. Tax laws must be modified in terms of professional and salaried employees. More tax holidays can be provided for professionals upto 30 years of age. Some Integrated system must be in place to trace the income sources.

iii. It should be noted that in chapter VI A that is of deductions where there is no need to upload the receipt of or any proof regarding that deduction has to be uploaded which is totally unfair because some are really incur those expenses which gives them deduction benefits and some does not incur such expenses but takes the deduction benefits because no evidence has to be uploaded on the IT site regarding that deduction. For e.g. in 80C if someone wants to claim deduction on LIC no receipts of such LIC has to be uploaded on the IT website. If that person is actually taking the LIC then it is ok but if not then it is unfair and tax evasion.

vi. The deduction for preventive health checkup has a limit of Rs. 5,000 in section 80D where if the amount of Rs. 5,000 is paid in cash is also allowed. Here this Rs.5,000 should also be allowed only when it is paid by cheque.

v. If a non-resident is not paying the taxes in which the income is earned but if that person is transferring such income to our country to his family or for any other purpose then the taxes must be levied on such transfer too. In short, taxes must be levied for transfer of the income also.

vi. Interest on IT refund must be exempted from tax because of the fact that it is not an income for the assessee. Because if the money of the assessee will not be blocked by the govt then he can earn more money by investing such money in profitable instruments. The first problem here is that govt blocks the money and the interest rate is very low and on that also they are charging tax which is totally unfair on part of assessee.

vii. By the virtue of section 10(17) Daily allowances received M.P. or M.L.A the actual amount received if exempted from tax. It is ok that they are rendering services to govt of India therefore their allowances are exempted but there must be some limit should be there. Because the corrupt M.P. OR M.L.A. takes their whole income in allowances only. Therefore there must be some limit on it.

viii. According section 10(10) Gratuity is fully exempt for govt employee which is fully partial and unfair for the private employees. It should be either exempt for both or taxable for both but it is wrong that taxable for private only and govt employee will be fully exempt.

ix. According to specific provision contained u/s 10(10A) commuted pension will be fully exempt which is again a matter of partiality with private employee.

x. According to section 10(10AA) Leave Encashment is fully exempt for govt employee which is again a matter of partiality with private employee.

6. Suggestion to individual tax payers regarding tax planning:

i. The assessee tries to increase to earn those incomes which are fully exempt from tax.

ii. The assessee tries to increase to incur those expenses which give them deduction benefit.

iii. The assessee tries to increase to investment in all those instruments which gives them deduction as a tax benefit.

iv. According to section 54 EC where the assessee gets deduction for purchasing the house against the capital gains. Here the points which should be noted that the purchased house must be on the name of that assessee on which the capital gains are arise. At the time of making investment the assessee must be knowing the deduction chapter in deep because the investment are planned in such a way that it gives full benefit of Rs.1,50,000 u/s 80C and 80CCC and they also get the benefit of deduction u/s 80CCB.

vi. Tax should be planned for salaried employees in such a way that they can take salary in way of exempt perquisites and in allowances which should get deduction benefit.

vii. An employee not getting HRA then if he is staying with his father and the house is on the name of his father then he can pay rent to his father and get deduction u/s 80GG. It is on assumption that his father is above 60 years of age and tax slabs applicable for him is different from him.

viii. A salaried individual must ensure that dearness allowance must be covered under terms of employment and forms basic salary. Because on the basic salary house rent allowance, Gratuity, commuted pension and contribution towards recognized provident fund will also be less taxable.

ix. A salaried individual must ensure that commission must also be covered under terms of employment but at a fixed percentage then it will also falls within the salary or it also forms basic salary.

- x. An employee should always get commuted pension because Uncommuted is fully taxable.
- xi. Tax on retirement benefits like gratuity is lower if they are paid in the beginning of the financial year.
- xii. If an assessee has more than one house then he should select that house as self- occupied property whose gross annual value is higher.
- xiii. If an asset for the purpose of business purchased by installments, then the assessee firstly can claimed deduction u/s 32 and a part form this the interest payable on unpaid purchase price can also be claimed as a deduction.
- xiv. An assessee must try to plan its transfer or sale of capital assets on or after 12 months if listed because it then becomes a long term capital assets and gives indexation benefits.

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