

India's Income Tax law revision: Well begun is still only half done

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The draft tabled simplifies its language but we also need changes that go beyond form to address key aspects of substance



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There has been significant press coverage of India's Income Tax Bill, 2025, which was introduced in Parliament on 21 July. As readers would recall, a committee was set up in October 2024 for the simplification of the Income Tax

Act; the panel's mandate was ring-fenced to simplification of language, reduction of litigation and the compliance burden, and the removal of redundant or obsolete provisions. In that sense, the committee was restrained by its limited mandate.

A Lok Sabha Select Committee was set up to look at the draft Income Tax Bill framed by the Simplification Committee, which has submitted its report with 285 recommendations, a majority of which seem to find favour with the government; the net result is that the bill framed by the simplification panel will likely be passed into law with some changes. However, there are some key aspects that need to be discussed.

The Income Tax Act of 1961 has been amended dozens of times, and with some 4,000 amendments, its language had turned complex; in this context, the simplification panel has made a good attempt to offer clarity. For example, several tables and explanations have been added and the number of sections has been brought down from 819 to 516. However, there are concerns over several aspects; for example, there has been a tendency to delegate rule-making to the Central Board of Direct Taxes (CBDT)—like in the case of faceless assessments—whereby, compared to existing provisions, the CBDT would gain greater scope to make legislative-type changes without parliamentary oversight. This is worrisome.

There are apparent errors and omissions in the existing law that should have been corrected. For example, in the context of the 'deemed gift' provision u/s 56(2)(x), the definition of 'relative' for tax exemption does not expressly include reciprocity, or whether the relationship is mutually applicable for gifting; this aspect should have been explicitly clarified (even under the existing law, the CBDT should have issued such a circular). It impacts gifting between taxpayers and nephews, for example, if the tax exemption for relatives applies only one-way. Also, the tax neutrality provision for a 'demerger' does not include 'fast track demerger,' because that concept came later. Representations were received by the Select Committee and both these aspects were pointed out to the ministry, but were apparently brushed aside; surprisingly, the common-sense point that relationships should be reciprocal (or two-way) was met with a response from the ministry that this is "in the nature of a major policy change!"

Although the Committee's mandate was limited, the larger concern is that once the bill is enacted, the government would be reluctant to make sub-

stantive changes. Here are some we badly need.

Individual taxation: The limit of annual income beyond which the maximum tax rate kicks in is only ₹15 lakh, which seems too low and needs to be addressed. Also, medical expenses have gone through the roof in the last few years, as have education costs; both these are critical, and even relatively well-off Indians are struggling to meet these costs. The bill should allow a higher deduction for mediclaim and medical expenses and provide for a meaningful deduction for education (the latter could help address the skill gaps we face). Real estate costs have also shot up, while the deduction of interest on housing loans is too low at ₹2 lakh per year. This badly needs an upward revision.

Corporate taxation: India's corporate tax rate is very reasonable at 25%; however, some aspects that need to be addressed relate to mergers and acquisitions (M&As), including group restructuring. Some specific aspects that could be looked at even at this stage have been long-standing demands. The definition of a 'demerger' for tax neutrality is highly restrictive and needs rationalization. The commercial reality of M&A transactions involves earn-outs and deferred amounts, and the Act does not have contemporary provisions on the year of taxability, which causes uncertainty and litigation. Losses of merging companies are allowed to be carried forward only in restricted circumstances, primarily if the merging company is in manufacturing; this is a relic from a bygone era, since several service companies also have losses and the mergers of such companies could save them from extinction and prevent job losses.

India's problem of non-performing assets has reduced but is still substantial. In the context of takeovers that emerge from the official bankruptcy process, the provision in Section 28 that makes write-backs of haircuts taken by lenders taxable is a major dampener from the perspective of an acquirer that seeks to reduce its risk of acquiring an insolvent company to resurrect.

The last two aspects have again been pointed out to the ministry, which appears not to see merit in these changes.

Administrative dimensions: There have been simplifications in Tax Collected at Source (TCS) and Tax Deducted at Source (TDS), but the larger issue is that the deductor of tax is doing the government's job; from an Ease of Doing Business perspective, TDS provisions need to be shrunk, as opposed to language being simplified. Also, given the need to reduce tax litigation, a robust advance ruling mechanism needs to be put in place, so that tax disputes can be addressed upfront; all advance ruling mechanisms till now have failed, either because of faulty architecture or elongated time frames (or both), making the term 'advance' seem meaningless.

Given the Simplification Committee's mandate, it has done well to simplify the law's language, but unfortunately, that's about form rather than substance; the issues outlined above still need to be addressed in the context of India's avowed intent to ease business. At least some structural changes are needed. A redraft of our tax law is useful and attractive, no doubt, but would be disappointing if it falls short of dealing with fundamental issues.



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