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RESEARCH ARTICLE

TAXATION OF FAMILY INCOME UNDER INDIAN TAXATION LAWS A NEW PERSPECTIVE

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Abstract

Since the monarchy pattern of ruling the state to the republic era, one aspect is common i.e taxation. The revenue required for funding the public services and maintaining law and order, various types of taxes are imposed on citizens and organisations by the competent authority. In India, the taxation of income is the exclusive power of Central Government and The Income Tax Act 1961 is the governing Act for the taxation matter. The present paper is conceptual in nature. The author wants to propose a new scheme of taxation of family income. As per the author's proposal the combine income of the family will be charged to tax instead of charging individuals income separately. The authors has given the reference of few prevailing schemes to support his claim. Before writing the conclusion of the paper, the positive and negative aspects of the new proposal are also discussed. The idea behind the new proposal is to condense the disparity in disposal income of individual and family income.

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Introduction:-

Taxation is one of the important sources for the government of any country. Almost all countries in the world impose tax on individual and organizations as per taxation laws of the respective country. The present paper judgmentally reviews few existing provisions of the Indian taxation laws and propose a revision in one of the area. The Indian taxation system is three tier system bifurcated between Central Government, State Government and Local authorities. The Article 246 of The Constitution of India distributes the power to impose tax between Central Government, State Government and the local authorities. In India, the taxes are categorized into two types. The first is the direct tax. In direct taxes the liability of payment neither be pass-on to other person nor can tax-payable be recovered from third person. It is the taxpayer who is principally liable to pay the taxes. The second type is the indirect tax. In this type, actual taxes are paid by the end consumer whereas service provider acting as a medium of collecting and depositing the tax amount with the government. In Indian taxation system, income tax (tax on annual income of individual and organisations) falls under first category and Goods and Service Tax (GST) falls under the second. The direct taxes are governed by The Income Tax Act 1961 and the indirect taxes are governed by Goods and Service Tax Act 2017.

The taxation laws are continuously amended according to the economic situation of the country. Considering the present provisions in the Income Tax Act 1961, the author proposes an extension of the scope of the definition of person as defined in the section 2(31) of the Act. It is proposed that the taxation system should recognize "family" as type of person within the definition of section 2(31). As of now the individual members of the family are assessed to tax individually. As per the author's proposal, the individual income of all members of a family will be added as family income. Here the word family means individual and spouse. The other members of family like parents and

children are excluded from the definition due to expected ambiguity during implementation of the concept. The tax slab rate will be applicable to family income and not to the individual income of the member of family which is prevailing provision. The proposed change is expected to bring more equality among the taxpayers which is explained in the later part of this paper. The principle of equality is one of the taxation principle as documented by Adam Smith in *The Wealth of Nations* (1776). At the same time the new proposal will also increase the tax revenue for the government. The aim of new proposal is not to increase the adversity of any taxpayers. The sole intention is to bring comparative congruence among the different taxpayers of the country.

Few relevant schemes/policies prevailing in India to support the author's proposal:

The following discussion is an indication where the Government is assuming family as one unit to extend the benefits of various government schemes and economic policies. The Government of India is providing subsidized domestic gas cylinder (aka liquefied petroleum gas, LPG) to the citizens. In the year 2012, then ruling government restricted the usage of 6 LPGs per household every year. This limit was increased to 9 cylinder in January 2013. In the year 2014, the decision was again amended and 12 cylinder are allowed to consume per household. This move considers family as a unit and benefits of subsidy is restricted to a family as a whole and not to the individual member of family. Individual members staying together are not permitted to have more than one LPG subscription at one common address.

In another policy decision, the housing subsidy under Prime Minister Awas Yojna (PMAY)¹ is also restricted to only one member of the family including child member of the family. The housing subsidy is given to only first house purchased by any one family member. The subsequent purchase of house is not entitled the housing subsidy under PMAY. Here also family is the focal point to pass on the economic benefits.

These are the clear evidences that the government is considering family as a single unit while framing economic policies. On the similar backgrounds, the author of the paper wants to propose a new scheme of taxation of family under income tax act which is discussed in the following part of the paper.

Existing system of taxation of individuals and its comparative analysis:

The existing system of taxation of individual is depicted below with a hypothetical situation. Then it is compared with family income having more than one person as earning member of the family.

Situation – I

Let us assume an individual person earning total taxable income of Rs. 10,00,000 (aged less than 60 years). His tax liability will be Rs. 1,17,000 (as per tax rate applicable for AY 2020-21, including surcharge @ 4%). The disposal income of the individual is Rs. 8,83,000 (Income – Taxes, i.e. 10,00,000 – 1,17,000).

Let's assume there is one family having two individual persons earning Rs. 5,00,000 each. The tax liability of individual person is Rs. 0 (zero) after considering rebate under section 87A² of the Income Tax Act. Thus the total income of family is Rs. 10,00,000 and tax liability is zero. The disposal income of the family is Rs. 10,00,000 as there is no tax liability on any of the family member.

In another situation, (situation II) let us assume there is one family having two individual persons earning Rs. 7,50,000 each. The total family income will be Rs. 15,00,000. The tax liability of family is Rs. 1,30,000 (Rs. 65,000 each, as per tax rate applicable for AY 2020-21, including surcharge @ 4%). The disposal income is Rs. 13,70,000 (Income – Taxes i.e. 15,00,000 – 1,30,000).

Whereas the tax liability of individual person earning taxable income of Rs. 15,00,000 will be Rs. 2,73,000 (as per tax rate applicable for AY 2020-21, including surcharge @ 4%). The disposal income of the individual is Rs. 12,27,000 (Income – Taxes i.e. 15,00,000 – 2,73,000).

In situation I, the tax paid by individual is Rs. 1,17,000 and tax paid by family of two is zero. The difference between disposal income of the individual and family in situation I is Rs. 1,17,000. In situation II, the tax paid by individual is Rs. 2,73,000 and taxes paid by family is Rs. 1,30,000 and difference between taxes paid by individual

¹ For more information <https://pmaymis.gov.in/>

² Income tax rebate up to Rs. 12,500 for individuals having taxable income up to Rs. 5,00,000.

and family is Rs. 1,43,000 (Rs2,73,000 – Rs1,30,000). In both the situations, an individual is paying more taxes than family and therefore having less disposal income whereas the total income (income before taxes) is same. In the opinion of the author this may prompt inequality among the tax payer having same income.

The problem statement:

The difference between tax liability of individual person and family of two is wide enough creating disparity in the disposable income as well as in the amount of taxes paid.

Can Tax laws truncate this disparity and bring more harmony between individual and family? **The proposal**

The author wants to propose the concept of taxation of family as one taxpayer. Under this proposal the family means an individual and spouse (hereafter referred as couple). The income of couple will be clubbed and tax rates will be applicable on the combined income of the two. The income will be declared by them jointly and a joint return will be filed by the both as long as their marital relationship subsists. As per the prevailing laws, few deductions (section 80D, 80DD) are allowed to any one member of the family. The same provision will be continued in the new proposal. The separate deduction can be allowed to both the family member in certain cases like investment in public provided fund and life insurance policies taken on individual life. The gross total income of the two family members is proposed to calculate individually. However while calculating tax liability, the exemption limit will be applicable to the combined income of husband and wife and not to the individual as per the prevailing provision. The children (minor or major) are excluded from the definition of family.

This may not be the first case where taxpayer will experience the increase in comparative tax liability. As per Indian tax laws, the agriculture income is exempted from tax under section 10(2) of the Income Tax Act 1961, however it is added to non-agricultural income for rate purpose. This is called as partial integration of agriculture income or indirect taxation of agriculture income. Under this method the agriculture income is added to non-agricultural income which always result in higher tax liability of taxpayer having agriculture income as well as non-agricultural income. In short, the agricultural income is not fully exempted from income taxes but it is added to non-agricultural income for rate purpose.

Implication of new proposal:

The proposal aims to bring the equality among the taxpayers. In the opinion of the author and referring to the calculations as depicted in annexure I, the individual with taxable income of Rs 10,00,000 with tax liability of Rs 1,17,000 is at a highly detrimental position as compared to a family having same amount of income with zero tax liability. This may create displeasure among the taxpayers. If the family of two (individual and spouse) is considered as person and taxation is done as per proposed method, more equality can be attained between the taxpayers as the benefits of income earned separately will be enjoyed jointly by them. Thus the gap between tax paid by an individual and tax paid by individual members of family will be narrowed down. The aim of the new proposal is to consider family of two as one taxpayer and bring equality among taxpayers. Though it is not the object of this proposal, the Government will also witness the increase in the revenue due if the proposal is implemented.

Punitive side of the new proposal:

The tax payers who are assessed as now individually will be assessed as a family under the new proposal. They will be forced to shift from nil brackets to taxpayer category or from lower tax bracket to higher tax bracket. More importantly, the minimum exemption limit which is available to individual member of the family will be available to family as a one unit. This will definitely increase the tax liability of the family. Due to outflow of cash on account of increased tax liability, they may oppose the new proposal. Even political willingness is to play a big role to propose the new scheme of family taxation. However, such unpleasant provisions are not new in the taxation. The Act has introduced Alternate Minimum Tax (sec. 115JC), Taxation of capital gain (section 112) which was earlier exempted, taxation of dividend (section 10(34)) in the hands of retail shareholder which is exempted up to Rs. 10,00,000 are few instances where tax liability of the taxpayers had increased substantially due to changes in the tax laws. In the opinion of the author, such amendments are required to reduce the uneven tax liability among the individual person and total family income. The positive outcome may be observed if we look such changes from broader economic perspective.

Conclusion:-

The author has come up with a new proposal of taxation of family income in India. Here the term family includes married couples only. Children and parents are excluded from the concept of family due to foreseen operational

difficulties in the implementation of the concept. The proposal is to combine the income of individual and spouse. The tax bracket and minimum exemption limit is proposed to be applicable to the combine income and not to the individual. The sole intension of the proposal is to minimize the disparity in disposal income of the individual as income of family as per new definition. If the proposed concept implemented, the principle of equality of taxation will be achieving a greater height in the Indian taxation system.

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