

THE BUDGET PROPOSALS

1985/86

THE TAXATION MEASURES

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The Minister of Finance and Planning has generously granted a variety of tax concessions and benefits so that every conceivable class of tax payer would have reason to be joyous. However, this show of generosity has been motivated by a desire to woo and win the delinquent tax payer over from his crooked ways of evasion.

The Minister claims that by reducing the Turnover Tax Rate from 4% to 1%, the revenue from Turnover Tax has increased. He is therefore confident that reduction of the Income Tax rates would have the same beneficial results.

The Minister has also given consideration to the annual rate of inflation and endeavoured to give some measure of relief by ensuring a reduction in tax by increasing Personal Allowances and widening the slabs.

The Proposals

1. Increase of Personal Allowance from Rs.18,000 to Rs.24,000.
2. Widening of slabs from Rs.6,000 to Rs.9,000.

Present rate schedule

First Rs.200,000	exempt
Next Rs.200,000	exempt
Next Rs.500,000	3/4%
Next Rs.1,000,000	1%
Balance	2%

3. Abolition of Surcharge and Rehabilitation Levy.
4. Raising the exemption limit from Rs.50,000 to Rs.100,000 in respect of Gratuities.
5. Permitting deduction of gratuities paid to employees on closure of business.
6. Granting of 1/2 tax holidays to export industries for a period of five years after the expiry of the initial 5 year tax holiday.
7. Qualifying Payment Relief for Investors in labour intensive industries in selected areas.
8. Extending exemption provisions for NRFC Account holders.
9. Limitation of Qualifying Payment Relief to 1/3 Assessable Income or Rs.500,000 whichever is lower.
10. Abolition of allowance for annuities except those on order of court.
11. Raising rate of tax on executors.
12. Exemption of dividend income upto Rs.12,000.
13. Wealth Tax - Reduction of rates and widening of slabs are as follows :

Proposed rate schedule

Rs.500,000	exempt
Rs.500,000	exempt
Rs.1,000,000	3/4%
Rs.1,500,000	1%
Balance	2%

14. Stamp Duty - Reduction of rates on transfer of property are as follows:

Present Rates	Proposed Rates
Value of Property	Rate
Less than Rs.50,000	3%
Rs.50,000-100,000	5%
Over Rs.100,000	6%

EXAMPLE : B Income Rs.100,000

	1983/4	1984/5	1985/6
	Rs.	Rs.	Rs.
	100,000	100,000	100,000
	<u>12,000</u>	<u>18,000</u>	<u>24,000</u>
	88,000	82,000	76,000
Highest Slab	<u>52,800</u>	<u>66,000</u>	<u>72,000</u>
	34,200	16,000	4,000 @ 45%
Tax	15,600	19,500	16,425
	<u>18,810</u>	<u>8,800</u>	<u>1,800</u>
	34,410	28,300	18,225
Saving over Previous year	(6,110)	(10,075)	

15. Computerization of information to be better equipped to deal with evasion.

Rs.24,000 and Rs.100,000 stands to benefit by this measure of relief.

Below are a few impressions on the probable effects of some of the proposals. It is hoped that the brief discussion that follows will stimulate the reader to make a deeper analysis.

Hence increase in income available for spending as a result of the proposals is insignificant.

If a man earns Rs.100,000 his spendable income after deduction of tax will be as follows:

Personal Allowances and Widening of Slabs

In order to make allowance for the annual rate of inflation the Minister of Finance has indicated that annual review of the Personal Allowances and Slabs is necessary. However, due to the need to maintain Income Tax as a major source of Revenue the Minister has merely increased the Personal Allowance from Rs.18,000 to Rs.24,000 and widened the slab of Rs.6,000 to Rs.9,000. The major sector of the tax paying public being the middle income earners whose income is between

	1983/84	1984/85	1985/86
	Rs.	Rs.	Rs.
Spendable income			
if income Rs.100,000	100,000	100,000	100,000
	<u>34,410</u>	<u>28,300</u>	<u>18,225</u>
Spendable Income	<u>65,590</u>	<u>71,700</u>	<u>81,775</u>
if income Rs.24,000	24,000	24,000	24,000
	<u>1,200</u>	<u>450</u>	<u>-</u>
Spendable Income	<u>22,800</u>	<u>23,550</u>	<u>24,000</u>

EXAMPLE : A Income Rs.24,000

	1983/4	1984/5	1985/6
	Rs.	Rs.	Rs.
Taxable Income	24,000	24,000	24,000
Tax	<u>12,000</u>	<u>18,000</u>	<u>24,000</u>
Spendable Income	<u>12,000</u>	<u>6,000</u>	<u>Nil</u>
Income	1,200	450	Nil
Less Tax	<u>22,800</u>	<u>23,550</u>	<u>24,000</u>

A Rs.24,000 annual income earner does not appear to have been given a real benefit in terms of an increase in the light of inflation.

An increase of the Personal Allowance to Rs.30,000/- would not have strained the source of revenue as the resultant loss would have been only Rs.1,050/- per tax payer. (See example on page 16)

EXAMPLE: Income Rs.30,000

	1984/5	1985/6 "Proposed"
	Rs	Rs.
Income	30,000	30,000
Personal Allowance	<u>18,000</u>	<u>30,000</u>
	12,000	NIL
Tax	1,050	NIL
Spendable Income	28,950	30,000

Annuities – Disallowed

An annuity is an annual charge against income and has been always allowed by the Inland Revenue Law. However, from time to time the Department has restricted its allowance. More recently the Inland Revenue Act, as amended by Act No. 24 of 1980, permitted the deduction of annuities if it was for a period longer than 6 years or if it was for consideration or the life of the annuitant.

Recourse was had to this allowance as it was a legitimate way of deducting from one's income the annual contribution which a dutiful son or brother or sister made towards the cost of running the family home or sharing the cost of secondary or tertiary education. In other words expenditure on one's family members which is not deductible could have been deducted on converting it into a charge on a legal document duly stamped. Now, however, after its disallowance the expenses will still be borne by the children and brothers or sisters without the benefit of a deduction. This disallowance however will not be as harsh as it would seem at first sight, because the Minister for different reasons has chosen to enlarge the Personal Allowance from Rs.12,000 to Rs.24,000 and widen the slabs from Rs.6,000 to Rs.9,000 and thus mitigate the consequences of the disallowance.

Annuities - Allowed

The Minister has chosen to allow annuities payable on orders of Court by a spouse or parent.

It would normally appear that alimony and other charges ordered by Court are made because either the spouse or the parent has failed in his duty and is guilty of some misdemeanour. Hence by granting a deduction (in case of a spouse guilty of adultery or neglectful parent) the Minister has chosen to mitigate the consequences of a Court Order by allowing the charge of annuity to be deducted from income.

Information

The proposal to computerize the Information Branch is probably a means of assisting the clerical staff of the Information Branch to collect information and route it to the assessing files if any or to the officer in the hope that a file would be opened.

Though this might be a god-send to the Information Branch the effect it would have on the Assessing Branches and the taxpayer have not been foreseen or calculated.

A probable effect would be the avalanche of information that will smother the Assessor incapacitating him from making a proper assessment or even from assessing the

importance of the information. As a result of this over-flow or avalanche - of information the spate of estimated assessments and appeals will increase in geometrical proportions.

Making assessments from applications for Letters of Credit may sound absurd but it does spell nonsense if an Assessor is expected to reconcile the purchases account with the Letters of Credit only in an endeavour to verify the return. Would not the Customs entry regarding imports have been better.

Exemption of Dividend Income upto Rs.12,000

The average rate of dividend declared today is between 5% and 10%. Hence in order to earn Rs. 12,000/- dividend on Rs.10 shares bought at par the outlay should be Rs.240,000. Hence an investor of Rs.240,000 besides claiming a Qualifying Payment and thus reducing his tax considerably is given further relief. Furthermore, is an investor of Rs.240,000 a small taxpayer? It is also common knowledge that most of the investors of recent times have been investing in Tax-Holiday Companies which have not declared dividends as yet and even if they do declare dividends the dividends would be exempt from tax. Hence it is not understood whom this exemption would benefit. It must also be mentioned that the cheapest, simplest and most popular form of investment is the Savings Bank or Finance Company. Deposits resorted to by small investors.

Increase of Executor's rate of tax by 10% from 30% to 40%

While conceding that if the beneficiary has reached the 55% slab it would be a saving (see examples below) to have the income from the Estate taxed at 40% it is not reasonable to expect an Estate to be kept open in that manner. In any case the Inland Revenue Department appears to have usurped the functions of the

District Court in whom the authority and power to supervise the administration of estates is vested.

Section 63 (4) reads as follows "Where the income or net wealth to which a beneficiary is entitled from the estate of a deceased person **CANNOT BE ASCERTAINED** the executor shall be chargeable with income tax or wealth tax in respect of such income or wealth". Thus only in those cases where the Assessor cannot ascertain the beneficiary's entitlement can an assessment be made on the executor. One shudders at the inability of an Assessor to ascertain the entitlement of a beneficiary. In a department overflowing with talent and training one cannot imagine that there could be more than 10 such cases in a period of 10 years. The effect of this provision, however, may be a comfortable excuse for the Assessor to postpone ascertainment rather than a measure to prevent avoidance of tax by beneficiaries of an estate. However, it is more reasonable to expect difficulty on the part of the beneficiaries to resolve disputes quickly in the present system of law's delays so that imposition of a higher rate may result in hardship to the heirs of an estate, which cannot be 'distributed' by the assessor.

Granting of 1/2 tax holidays which in effect means permitting the industries to pay only 50% of the tax assessed for a further period of 5 years to enable them to stay in business. No one will complain about this because this concession would not be granted indiscriminately but only to those industries which have a net foreign exchange earning acceptable to the Export Development Board.

Labour Intensive Industries Investment Relief

The granting of investment relief to investors in labour inten-

EXAMPLE 1

A is a Mercantile executive and his income is as follows for the year ending 31.3.84.

Remuneration	Rs.102,000		
Share of deceased father's estate	38,000		
	140,000		
Tax is recomputed as follows	102,000 @ 50%	=	30,675
	38,000 @ 55%	=	20,900
		Total Tax =	51,575

EXAMPLE II

Same as above except that the income from the deceased father's estate is assessed on the Executor and not in him because estate is treated as not having been distributed. Hence,

1) Tax on Salary of Rs.102,000	=	30,675
2) While Executor pays tax on Rs.38,000 @ 40%	=	15,200
Total Tax = 30,675		
15,200	Saving =	5,700
If tax was @ 45,875		
30% before amendment	the saving would have been =	9,500

sive industries is certainly one means of providing employment and training in backward areas but as has been experienced the profit earning capacity of labour saving industries compared with industries using machinery is low and this fact coupled with the poor infrastructure available in those areas and the high cost of transport, besides the welter of labour legislation, could dissuade any investor from investing in those projects. Further, the poor performance of the various projects in industry and tourism have brought about a climate of diffidence in investment, so that much more would have to be done to restore confidence in the investor.

Gratuities - Raising of Exemption Limit from Rs.50,000 to Rs.100,000

This is certainly a measure of relief to a person retiring and hoping to make provision for the fading years of his or her life.

In conclusion it might be said that the Minister's proposals would be welcomed by all taxpayers except those who feel a nostalgia for annuities. But the question still remains whether despite these kind and generous offers voluntary compliance on the part of the taxpayers will improve without a determined and sustained effort on the part of the Department of Inland Revenue to 'persuade' taxpayers.