
# Abolition of Dividend Distribution Tax – An Impact Analysis

*By*

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# OBJECTIVES OF DIVIDEND DISTRIBUTION TAX – INTRODUCTION & ABOLITION

## DDT - INTRODUCTION

- Collection of tax is administratively easier being at a single point.
- Reduced compliance burden on issuing companies with respect to issue of withholding tax certificates.
- Receipt of tax revenue is assured , including from non-residents.

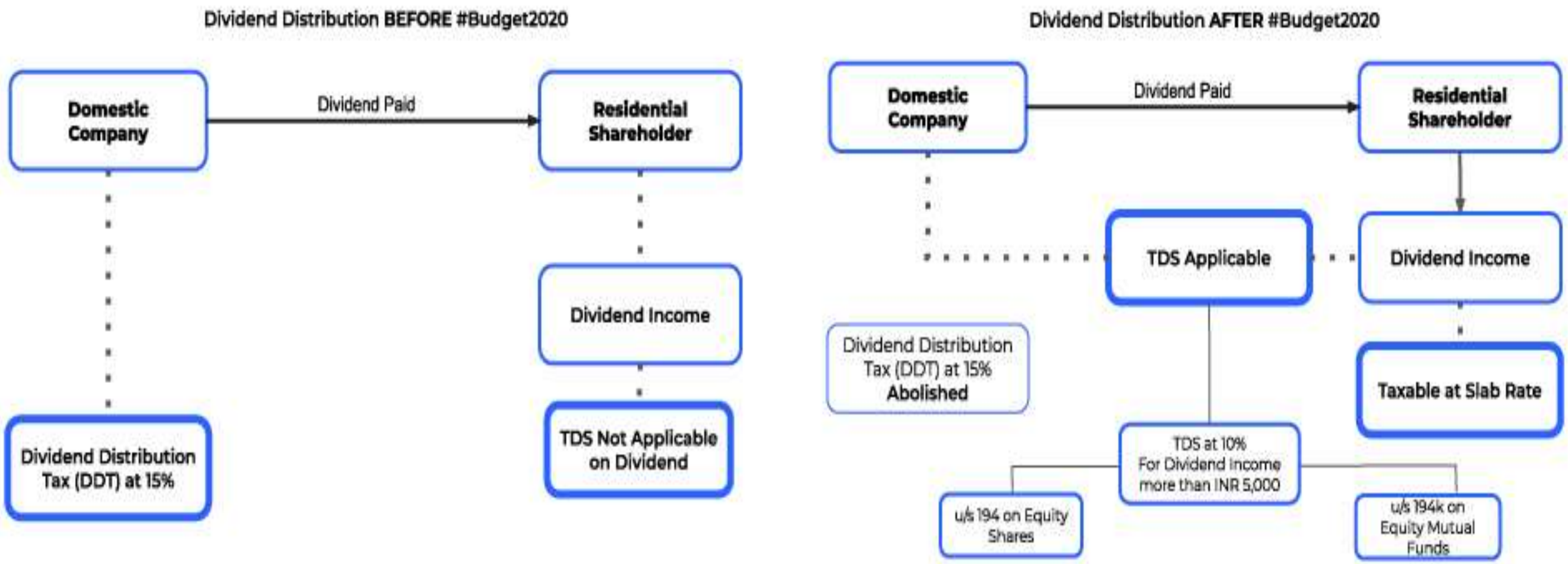
## DDT - ABOLITION

- Burdensome as companies are required to pay this tax in addition to the corporate tax payable on its annual profits.
- Regressive as DDT is levied at a flat rate on the distributed profits, irrespective of the marginal rate at which the recipient is otherwise taxed
- Relief to foreign equity investors in the form availability of tax credits and also applicability of DTAA.

# DIVIDEND DISTRIBUTION TAX – PAST & PROPOSED

HIGHLIGHTS BUDGET-2020

## TAXABILITY OF DIVIDEND - DIVIDEND DISTRIBUTION TAX (DDT)



# DIVIDEND DISTRIBUTION TAX (DDT)

## Current Scenario

- ✓ If any investor receives dividend in respect of investment made by him in any domestic company or units of a mutual fund then he shall not be liable to pay any tax on such dividend by virtue of exemption u/s 10(34) and 10(35) of the Act.
- ✓ The distributing company or the mutual fund shall be liable to pay distribution tax u/s 115-O and u/s 115R.
- ✓ No dividend distribution tax payable in case of dividend paid to Business Trust or by a co. in IFSC.

## Proposed in Budget 2020

- ✓ No DDT shall be payable by the company or mutual fund on any dividend distributed on or after April 1, 2020 – Section 115-O and Section 115R are proposed to be amended. However, income of a mutual fund shall continue to be exempt u/s 10(23D) though it would not be liable to pay distribution tax.
- ✓ Tax on dividend shall be levied in the hands of shareholders or unit holders – Sec 10(34) and Sec 10(35) which provides exemption in respect of dividend receipt by shareholders and unit holders are proposed to be amended.

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## Proposed in Budget 2020

- ✓ Taxability of dividend received by unit holders from Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InVITs) – Consequent amendments proposed to Sec 10(23FC), 10(23FD) and Sec 115UA.
- ✓ Deduction in case of inter-corporate dividends where a domestic company receives dividend from another domestic company – New Sec 80M proposed to be inserted.
- ✓ Sec 57 is proposed to be amended to claim deduction of interest incurred to earn dividend income subject to the limit of 20% of the dividend income. Commission or Remuneration to Banker for realisation of such dividend not allowed.

# TDS PROVISIONS APPLICABLE ON DISTRIBUTION OF DIVIDEND OR INCOME ON UNITS

| Section | TDS Provision |
|---|---|
| **194** | Deduction of tax at source on distribution or payment of dividend by an **Indian Company**. Rate of Tax 10% . If dividend distributed or paid to shareholder exceeds Rs 5000. |
| **194LBA** | Deduction of tax at source by Business trust on dividend income paid to unit holder. Rate of tax 10% if dividend paid to resident unit holders. For Non-resident unit holders, the rate of tax shall be 5% for interest income and 10% for dividend income. |
| **194K** | New Section proposed for deduction of tax @ 10% if any income exceeding Rs 5000 is paid to a resident<br>▪ In respect of units of a Mutual Fund specified u/s 10(23D)<br>▪ Units from the administrator of the specified undertaking or<br>▪ Units from the specified company. |
| **195** | Deduction of Tax at source from payment of dividend made to Non-resident |
| **196A** | Deduction of Tax at source from income payable to Non-resident unit holders in respect of units of mutual fund. |
| **196C&196D** | TDS @ 10%on dividend in respect of Global Depository receipt. TDS @ 20% in respect of securities referred to u/s 115AD. |

# PERSONAL TAXATION- INDIVIDUALS & HUF

## Tax Rates for an Individual ( Non-Senior Citizen)

| Total Income ( Rs ) | New Regime | Old Regime |
|---|---|---|
| Upto Rs 2,50,000 | - | - |
| Rs 2,50,000 to Rs 5,00,000 | 5% | 5% |
| Rs 5,00,000 to Rs 7,50,000 | 10% | 20% |
| Rs 7,50,000 to Rs 10,00,000 | 15% | 20% |
| Rs 10,00,000 to Rs 12,50,000 | 20% | 30% |
| Rs 12,50,000 to Rs 15,00,000 | 25% | 30% |
| Above Rs 15,00,000 | 30% | 30% |

1) **Taxpayer opting for New Tax Regime shall not be entitled to claim specified exemption and deduction.**
2) **A Resident Individual whose Taxable Income does not exceed Rs 5,00,000 can claim a taxable rebate u/s 87A. The amount of rebate shall be lower of 100% of the Income tax or Rs 12500. It can be claimed under both New and Old Tax Regime.**

# DIVIDEND DISTRIBUTION TAX (DDT) – IMPACT ON SHAREHOLDER'S EARNING

| **Shareholder** | **Current Tax Rate** | **Financial Year 2019-20** | **Financial Year 2020-21** | | | **Net Benefit/ Loss #** |
|---|---|---|---|---|---|---|
| | | Dividend received after DDT@ 20.55% | Dividend Received* | Tax on Dividend | Net Inflow from Dividend | |
| Mr A | 5.20 % | 1,00,000 | 1,20,555 | 6,269 | 1,14,286 | **14,286** |
| Mr B | 10.40% | 1,00,000 | 1,20,555 | 12,538 | 1,08,017 | **8,017** |
| Mr C | 15.60% | 1,00,000 | 1,20,555 | 18,807 | 1,01748 | **1,748** |
| Mr X | 20.80% | 1,00,000 | 1,20,555 | 25,076 | 95,480 | **4,520** |
| Mr Y | 26.0% | 1,00,000 | 1,20,555 | 31,344 | 89,211 | **10,789** |
| Mr Z | 31.20 % | 1,00,000 | 1,20,555 | 37,613 | 82,942 | **17,058** |

**Assuming portion of distributable profit which was utilised for payment of DDT – till FY 2019-20, shall be distributed among shareholders.**

**# Inspite of increase in the amount of dividend from Rs 1,00,000 to Rs 1,22,055 , the Net impact is favourable tax brackets i.e. 5%, 10% & 15%. For all others it will amount to net loss.**

# IMPACT ANALYSIS ON ABOLITION OF DDT ON RESIDENT SHAREHOLDERS

- ✓ With the abolition of DDT , the net benefit on account of taxation in the hands of low income group ( ≤ ₹5,00,000 ) will be higher by about 14% . This reduction in the tax burden along with expected increased flow of dividend distribution from the corporate sectors will hopefully boost the investment attitude of the small investors and hence will impact capital market favourably.
- ✓ The same action envisaged amongst the middle income groups with incomes ₹ 5 Lakh - ₹ 7.5 Lakh and ₹ 7.5 Lakh - ₹ 10 Lakh.
- ✓ However, the abolition of DDT will have an adverse impact on the high income groups i.e. with income higher than 10 Lakhs.
- ✓ Similar impact is expected in Mutual Fund Debt Market with abolition of DDT ( 29.12%) which may lead to a positive lift in the Debt Mutual Fund Market in India.

# IMPACT ANALYSIS ON ABOLITION OF DDT ON NON-RESIDENTS & FOREIGN PORTFOLIO INVESTORS

- Proposed omission of the second proviso to sec 195, thus dividend income earned by a non-resident shall be governed by the provision of section 195 and would be subject to withholding tax.
- With the introduction of withholding tax on dividend distributed to non-residents & foreign portfolio investors they will get the credit of the dividend tax paid in India at the time of filing their return.
- Withholding tax rate applicable under section 195 is the rate as per the Income Tax Act or the rate as per DTAA whichever is beneficial. In most of the cases where DTAA has been entered into, the beneficial rates vary between 5 – 15% which is below the 20% rate specified u/s 195.
- Also in certain DTAAs, two rates have been agreed wherein a further favourable rate is provided for recipient holding shares above specified percentages. Eg for Singapore it is given as below –

| **Country** | **Dividend (not being covered under Section 115-O)** | |
| --- | --- | --- |
| | **Tax Treaty** | **I-T Act** |
| **Singapore** | **a) 10%, if at least 25% of the shares of the company paying the dividend is held by the recipient company;<br>b) 15%, in other cases** | **20%/10%** |

# Impact Analysis on Abolition of DDT on Non-Residents & Foreign Portfolio Investors

- Moreover, for a non-resident it is always beneficial to apply the provisions of DTAA since even if DTAA says 20% , it will be inclusive of surcharge and cess .
- A non-residents will be eligible to apply for a certificate for lower withholding tax deduction in case the relevant DTAA provides for a lower withholding tax.
- However, India is a signatory to the Multilateral Convention (MLI) recommended by OECD to prevent Base Erosion and Profit Shifting. According to it, with respect to dividend income a minimum period of 365 days for which a shareholder, receiving dividend income, has to maintain its shareholding in the company paying the dividend to get the benefit of the reduced tax rate on the dividend.

# INTER-CORPORATE DIVIDEND – SEC 80M

## DOMESTIC COMPANY RECEIVES DIVIDEND FROM ANOTHER DOMESTIC COMPANY

- Inter-corporate dividend shall be reduced from total income of company receiving the dividend, if the same is further distributed to shareholders one month prior to the date of filing of return.
- This provision removes the cascading effect of tax.

## DOMESTIC COMPANY RECEIVES DIVIDEND FROM A FOREIGN COMPANY

- Dividend received by a domestic company from a foreign company, in which such domestic company has 26% or more equity shareholding, is taxable at a rate of 15% plus surcharge & HEC u/s 115BBD. Such tax shall be computed on gross basis without allowing any deduction for any expenditure.
- Dividend received by a domestic company from a foreign company, in which equity shareholding of such domestic company is less than 26% is taxable at normal tax rate. The domestic company can claim deduction for any expense incurred for the purpose of earning such dividend.

THANKS FOR WATCHING