Statutory Tax Rate in India V/s Select Countries

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Abstract

The corporate sector in India is characterised by the coexistence of Indian and foreign companies (the latter henceforth foreign direct investment companies or **FDI** companies), we examine the tax behaviour of these two segments separately. To supplement the analysis of **FDI** companies, this note further examines the behaviour of companies from eight countries, which account for the bulk of- **FDI** stock in India. This comprises seven countries from the Organisation for Economic Co-operation and Development **(OECD),** which together accounted for 55.7% of total **FDI** stock in 2012, such as France (with 1.7% share in total **FDI** stock), Germany (5.8%), Japan (7.1%), Netherlands (4.8%), Switzerland (5.1%), United Kingdom **(UK)** (16.3%) and United States (us) (14.9%). Along with Mauri- tius's share of 26.5%, these eight countries account for 82.2% of total **FDI** stock in India.

Introduction

Prior to 1991-92, corporations in India were subject to a relatively high direct tax structure. The statutory tax rate **(STR)** faced by domestic companies was as high as 59.13% in 1980-81. Though **STR** was gradually reduced through the 1980s, it remained high at 54% in 1989-90. Realising that such high tax rates would impair companies' capacities to generate funds inter- nally, which in turn could limit their investment activities, the government provided a plethora of tax reliefs and concessions, mosdy linked to investment - such as the depreciation allowance, investment allowance, tax holidays, loss carry forward and so on.

Literature Review

In the early 1990s, the Tax Reforms Committee (chaired by Raja J Chelliah) recommended a reduction in rate. Taking cognisance of the tax rate spread of 24 countries, the committee considered a corporate tax rate of 40% as reasonable, though it was of the opinion that 35% would be attractive to investors. In line with the committee's recommendation, corporate **STR** has been gradually reduced since then. Simultaneously, with the reduction in corporate **STR,** several erstwhile tax concessions were discontinued, but depreciation allowance and tax holidays continued.

Methodology

This paper uses data extracted from the Reserve Bank of India (RBI) studies on company finance,, which is based on a sample of non government non financial pbulic and private companies, including FDI companies. Seprate data series for Indian and FDI companies have been derived using these RBI studies , based on the methodology proposed in Rajakumar (2014)

Table 1: Statutory Tax Rate in India V/s Select Countries

Years	India		United States	United Kingdom	Germany	Switzer land	Japan	Netherla nds	Franc e	Mauritius
	Domestic Companies	OtherThan Domestic Companies								
Average: 1992-93 to 1997-98	48.4	61.6	39.5	32.7	55.8	28.4	50.0	35.0	35.9	NA
1998-99 to 2002-03	36.8	48.0	39.3	30.2	47.6	25.4	42.0	34.9	38.3	NA
2003-04 to 201M2	34.7	42.0	39.2	28.9	35J	21.9	39.7	28.6	34.7	17.9

NA means not available.
Source: For India - Finance Bill, various Budget Documents.

In Table 1, we have mapped corporate **STR** in India along with those prevailing in the eight countries which account for a major share in total **FDI** stock. It can be seen in Table 1 that reduction in corporate tax rate had been the hallmark of corporate taxation policies of the last two decades in India. Another important feature is that different rates have been prescribed for "domestic companies" and "Other than domestic companies" with the **STR** of the latter remaining higher than the former, though the difference has narrowed over the years.[4] The **STR** of domestic companies used to be 23 percentage points lower than "Other than domestic companies" in 1992-93; in 2011-12 it was 9 percentage points lower.

Based on the movements of corporate **STR** in India, we have divided the entire period into three phases, namely, 1992-93 to 1997-98 (Period 1), 1998-99 to 2002-03 (Period 11), and 2003-04 and after (Period 111). The **STR** across the selected countries has come down over the years (Table 1). An international comparison of the average **STR** during these three periods shows that the average **STR** in India was 48.4% in Period 1 for domestic companies and 61.6% for "Other than domestic companies". Germany has an average **STR** of 55.8% in Period 1, which was higher than the **STR** of domestic companies in India. In all other **OECD** countries, **STR** remained low. With their reduction over the years, the average **STR** of domestic companies in India in Period 111 stood at 34.7%, which is less than the average **STR** in the us and Japan, but same as that prevails in France. Though the average **STR** in Germany is marginally high in Period in, the **STR** stood at 30.2% since 2008-09. A few counties like the **UK,** Switzerland and Netherlands have low corporate **STR.** Of all the countries reported, Mauritius has the lowest corporate tax rate - it was 25% in 2006 and 15% since 2008.'

Tax Incidence

Incidence of tax can be measured by effective tax rate **(ETR),** which is tax provisions expressed as a percentage of profit before tax **(PBT);**

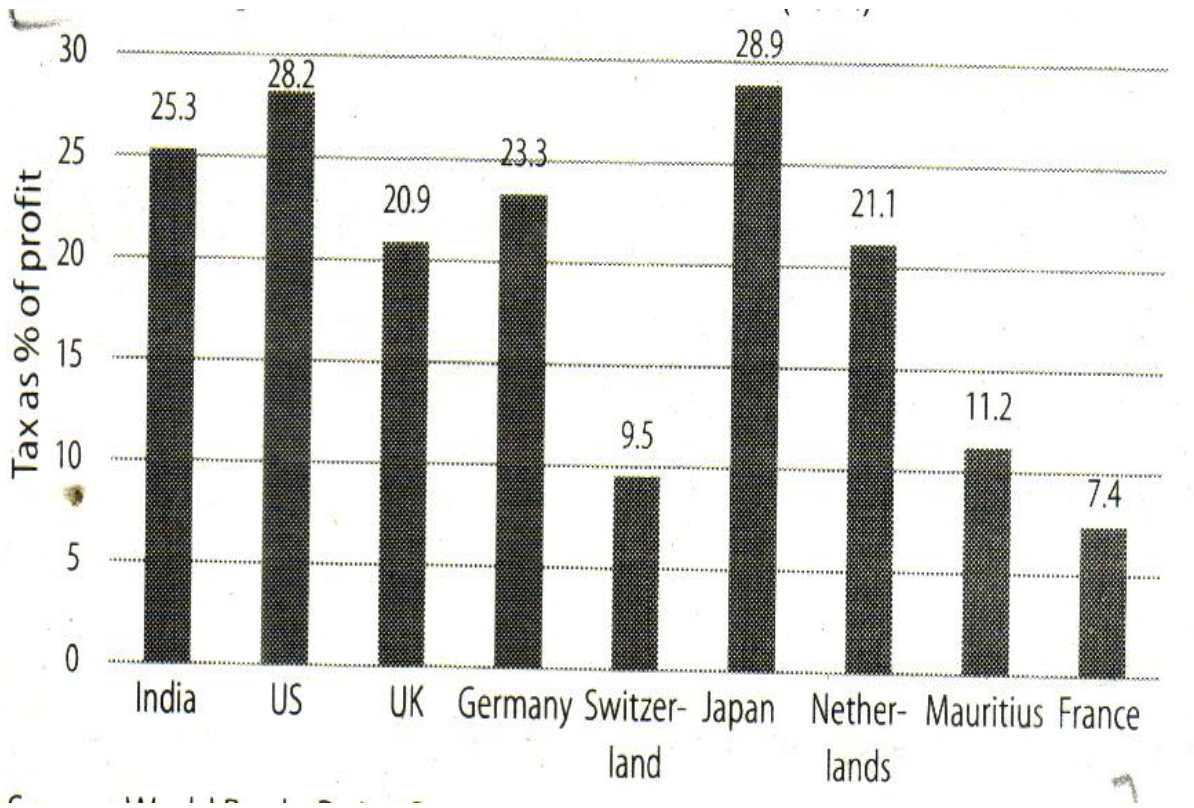
Years	All Companies	Indian Companies	FDI Companies	FDI Companies from							
				US	UK	Germany	Switzerland	Japan	Netherlands	Marits	France
Average											
1992-93 to 1997-98	25.1	21.3	36.8	38.5	37.6	42.6	33.8	29.8	41.8	34.3	NA
1998-99 to 2002-03	32.5	33.1	32.1	29.9	32.2	29.8	38.0	30.9	34.6	22.2	31.7
2003-04 to 2011-12	26.8	24.9	.31.4	30.0	32.5	35.6	34.0	38.7	33.1	22.7	35.9

NA indicates not available.
Source: Author's estimates based on data extracted from related RBI studies published in *RBI Bulletin,* various issues.

In Table 2, we have reported **ETR** of Indian and **FDI** companies, along with **ETR** of companies that belong to countries where **FDI** stock in India 2000-01 and 2002-03, fdi companies indeed had **ETRS** higher than that of Indian companies. In Period 11 only, the average **ETR** of **FDI** companies were less than Indian companies by 1 percentage point. For other periods, the **ETR** of **FDI** companies was more than Indian companies. The average **ETR** of **FDI** companies was higher than Indian companies by 15.5 percentage points in Period I, and the difference has narrowed to 6.5 percentage points in Period 111.

The **ETR** of **FDI** companies as a group has come down over the years and, in particular, the **ETR** of companies from the us, **UK,** Germany, Netherlands and Mauritius have drastically reduced since 2003-04.

Graph : Corporate ETR in SEect Countries (2014)



SOURCE : WORLD BANK. DOING BUSINESS 2015.

Corporate **ETR** in the select countries[7] is presented (Graph 1) to understand if companies from these important countries from an **FDI** point of view face higher tax incidence in India as compared to their home countries. Corporations in the us and Japan pay higher taxes on their ' un Period 111 as compared to Period 1. For profits than they would in India. In Indian companies, the ratio had doubled Germany, Netherlands and the **UK,** corporations have ETRs lower than India by some margin; wherein in Switzerland, Mauritius and France, they pay a very low percentage of their profit as tax. Graph 1 read along with Table 2 shows that **FDI** companies pay higher taxes as a percentage of their profit in India as opposed to what they would have to in their respective home countries. Only us companies pay almost the same portion ofprofit as tax in India and in their home.

In order to gauge the extent of tax incidence as opposed to what has been stipulated by the government, we have expressed **ETR** as a percentage of **STR**

TABLE3 : MEASUE OF TAX BURDEN

SAMPLE COMANIES OF	ETR TO STR			TAX PROVISION TO GVA		
	PERIOD I 1992 -93 TO 1997-98	PERIOD II 1998-99 TO 2002-03	PERIOD III 2003-04 TO 2011-12	PERIOD I 1992 -93 TO 1997-98	PERIOD II 1998-99 TO 2002-03	PERIOD III 2003-04 TO 2011-12
ALL COMPANIES	52.2	88.4	77.3	7.5	7.2	11.5
INDIAN COMPANIES	44.4	89.9	72.0	5.9	5.7	10.4
FDI COMPANIES	76.3	87.7	90.6	13.7	11.7	14.9
US	79.3	81.9	86.7	17.3	10.8	15.5
UK	78	88.2	93.9	15.9	16.0	19.2
GERMANY	89	80.7	102.6	11.4	8.8	18.1
SWITZERLAND	69.3	103.4	98.4	13.9	8.8	18.1
JAPAN	63.6	83.9	111.0	12.7	12.1	19.7
NETHERLANDS	89.4	94.2	95.6	11	6.9	12.3
MAURITUS	73.5	58.1	65.7	11.9	4.9	8.6
FRANCE	NA	87.6	104.1	NA	6.4	16.9

SOURCE : AUTHOR'S ESTIMATES BASED ON DATA EXTRACTED FORM RELATED RBI STUDIES PUBLISHED IN RBI BULLETIN.

Table 3, the ratio of **ETR** to **STR** has gone up in period in as compared to period 1. For Indian companies, the ratio had doubled between Period 1 and 11, when the **STR** rations have **ETRS** lower than India by of domestic companies was considerably reduced from an average of 48.4% to 36.8%. Although the average of the ratio of **ETR** to **STR** has declined in Period 111, it is still appreciably higher than the average of Period 1. A consistent rise in the ratio is noticed in the case of **FDI** companies as a whole and of companies from **OECD** countries except those from Germany, which recorded a decline in Period n. In sharp contrast to this, the ratio of **ETR** to **STR** of Mauritian companies had declined from an average of 73.5% in Period 1 to 58.1% in Period 11, only to rise to 65.7% in Period 111.

Does the overall rise in the ratio of **ETR** to **STR** imply that the share of taxes in corporate income has gone up? To examine this, we have worked out tax provision to gross value added **(GVA). AS** reported in Table 3, the relative share of tax in corporate **GVA** has marginally reduced during Period 11 when the **STR** had come down considerably. However, the share of tax in **GVA** has gone up in Period **HI**; the average tax share is 11.5% for corporations as a whole, as compared to the average of 7.2% of Period 11. The tax share has nearly doubled in the case of Indian companies between Period 11 and in from 5.7% to 10.4%. At the sector level, the reduction in **STR** has improved tax incidence and tax share in corporate **GVA,** particularly since 2003-04.

Conclusion :

With reduction in **STR,** there is an increase in the share of taxes in corporate **GVA** particularly since 2003-04, and concurrently the corporation tax as a percentage of **GDP** as a whole. While the behaviour demonstrated by Indian companies is different from **FDI** companies in terms of resorting to avoidance practices, both have shown improved tax compliance. It cannot therefore be denied that the reduction in **STR** has helped the government, to have a better share in corporate income

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