

India's Taxability of Individual equity Shareholders' dividend income from domestic companies

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Abstract - Since the instituting of the Income Tax Act, 1961, dividend income has been taxed in India under the heading of other sources. As a result of the many revisions made throughout time, taxation on dividend income has witnessed considerable turbulence. The way dividends are taxed has also changed. A dividend distribution tax was also imposed on domestic corporations whose earnings were either now being distributed to shareholders or had accrued in the previous year and were used to pay dividends to those shareholders. However, recipient shares are now again subject to tax on the distribution. This move would have wreaked havoc on both the stockholders who received their dividends and the firms that distribute their income. From 1997 through 2020, this paper looks at the tax treatment of dividend income from domestic corporations on equity shares in the hands of individual shareholders. Dividends are paid out to investors in the form of stock or mutual fund shares. Many of their stock and mutual fund assets pay out dividends to investors. That's why a lot of you are worried about whether or not you'll have to pay taxes on the profits you get from your investments. The taxation of dividend income is thus something that we should investigate more.

Keywords - Dividend, Dividend Distribution Tax, Dividend Tax, Individual, Equity Shareholders.

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INTRODUCTION

Profits from a company's equity and/or preference shareholders are often considered dividends in common terminology. It's also known as "passive income" or "unearned money," since it doesn't need any labour on the part of the recipient. In order to receive a strong dividend yield from a firm, one must put in a lot of work, or at least seek the assistance of an expert, to comprehend the company's financials. Taxing dividends has always been a priority for legislators due to the ease with which it may be earned as well as their worry about how the earnings dispersed ultimately end up being used. In India, dividends have been taxed in a variety of ways throughout the years. Solitary dividends on equity shares received by individual shareholders from domestic firms, starting in 1997, are examined in this research, since this was the time when India's corporate taxes underwent considerable reforms, and dividend taxation was also influenced greatly as a result of these reforms. To file a tax return, you may be unclear of how to account for dividend income. Is dividend income subject to taxation? The taxability of

dividend income was transferred from the hands of the firm that declared the dividend to the individual investors under the Finance Act 2020. We'll look at the new and old tax provisions on 'dividend income,' as well as the ramifications for taxpayers, in this post. A dividend from a company in India Now that the dividend distribution tax has been abolished, investors have more control over whether their dividend income is taxable or not. Dividend taxation under the old and new provisions.

DISCUSSION AND ANALYSIS

Until March 31, 2020, dividends received from an Indian corporation were tax-free (FY 2019-20). Payout tax had already been paid before payment was made by the corporation reporting such a dividend. A new system of dividend taxation was introduced in 2020 by the Finance Act of that year. All dividends received after April 1, 2020, will be taxed in the investor's account. Shareholder's Companies and mutual funds are no longer held liable for DDT. Additionally, the 10% dividend tax on dividends received by residents of India, HUFs, and enterprises above Rs 10 lakh (Section

115BBDA) has been abolished. Dr Naveen Prasadula. MSC (I.T), MBA, PHD (2018) Department of Business Management Osmania University Explained his study analysis on Dividends are paid out to investors.

1997: Shri P. Chidambaram noted in his 1997 budget address that taxation of dividends had been a contentious issue, and he planned to implement Section 115-O of the Income Tax Act, 1961, to resolve the conflict. A few corporations were cited that gave out enormous dividends, which he said was preferable to keeping the earnings and investing them to build their business. Companies who invested their earnings in long-term strategic expansion are rewarded in this section. By repealing Section 194 of the Income Tax Act, 1961, the Finance Act, 1997, effective June 1, 1997, eliminated the need for a tax at source deduction for dividends as defined in Section 115-O of the Income Tax Act, 1961. Since its inception, Chapter XII-D of the Income Tax Act of 1961 has dealt with "Special Provisions pertaining to tax on dispersed earnings of domestic enterprises" under the provisions of The Finance Act, 1997, which became effective on June 1, 1997. This chapter also included the introduction of sections 115-O to 115Q of the Income Tax Act, 1961. Income Tax Act, 1961's Section 115-O has always dealt with "Tax on dispersed earnings of domestic enterprises," from its commencement. Dividend Distribution Tax (DDT) of 10% was added to this new provision, which obliged domestic corporations to pay DDT on dividends declared, distributed or paid to shareholders from accumulated or current earnings. The Finance Act, 1997, however, eliminated the section 80L deduction advantage with immediate effect on April 1, 1998.

2000: Amendments to Section 115-O (income tax) were made on June 1, 2000 under Finance Act 2000, which increased the DDT rate from 10 percent to 20 percent. He suggested to boost DDT rates in his budget statement on February 29, 2000, in an effort to reduce the disparity in tax rates between interest and dividends and to counter the criticism that had been levelled against it.

2001: On June 1, 2001, The Finance Act, 2001 reduced the DDT rate from 15% to 10% by amending Division 115-O. Yashwant Sinha, the Honourable Finance Minister at the time, indicated in his budget address on February 28, 2001 that this measure was done to give our country's stock market a boost.

2002: The "rapport of Section 115-O of the Income Tax Act, 1961" were once again altered by the Finance Act, 2002, effective April 1, 2003, and this section was no longer applicable for the fiscal year beginning on April 1, 2002. That year, then-Finance

Minister Yashwant Sinha made a statement in his budget address declaring that the issue of dividend taxes had been worrying him during his term as Finance Minister and that he was ultimately persuaded that the current system of dividend taxation ought to be eliminated. As a result, he repealed the Income Tax Act of 1961's Section 115-O, removing the dividend income exemption and imposing tax on it directly on the recipient shareholders. Since the current dividend taxation system allows taxpayers in higher tax bands to deduct their dividend income and only tax such dividend income at a 10% rate under "the terms of Section 115-O of the Income Tax Act, 1961", he believed that it created unfairness.

2003: On February 28, 2003, Shri Jaswant Singh, India's then-honourable finance minister, proposed amending "Section 10 (34) of the Income Tax Act, 1961 to exempt dividends paid to shareholders" and to restore investor confidence in the equity and debt markets to encourage investment in India's industrial sector, improve equity and debt markets, and bring back retail investors to the market. On February 28, 2003, Shri Jaswant Singh, India's then-honourable finance minister, proposed amending Section 10 (34) of the Income Tax Act, 1961 to exempt dividends paid to shareholders and to restore investor confidence in the equity and debt markets to encourage investment in India's industrial sector, improve equity and debt markets, and bring back retail investors to the market. As a result, domestic corporations were compelled to pay DDT @ 12.50 percent on the amount of dividends declared, distributed, or paid out of their accumulated or current earnings under the Finance Act, 2003, which took effect on April 1, 2003. Due to the strengthening of Section 115-O of the Income Tax Act of 1961, Section 10 (34) of the Finance Act of 2003 reinstated excluding dividends from income tax. It was only a matter of time before Section 115-O of the Income Tax Act, 1961 was restored by The Finance Act, 2003, and Section 194 of the Income Tax Act, 1961 was removed from the public eye, making dividend income exempt from tax deduction at source. As of April 1, 2004, the Finance Act 2003 changed Section 80L of the 1961 Income Tax Act, effectively eliminating the deduction for dividend income received by individual shareholders from the tax bill. As of April 1, 2004, the Finance Act 2003 changed Section 80L of the 1961 Income Tax Act,

effectively eliminating the deduction for dividend income received by individual shareholders from the tax bill.

2007: The DDT rate was raised from 12.50 percent to 15 percent under Section 115-O of the Income Tax Act of 1961 by the Finance Act of 2007. There was a recommendation in the 2007 budget statement by Shri P. Chidambaram, the then Honourable Finance Minister, to raise DDT rates according to individual ability to pay while also encouraging vertical equity.

2014: As of October 1, 2014, the Finance (No. 2) Act, 2014 modified Section 115-O of the Income Tax Act, 1961, which required computing DDT scheduled the gross extra amount instead of the dividend amount net of taxes. To address this issue, then Finance Minister Shri Arun Jaitley suggested that dividends should be taxed on the total amount received by shareholders, while domestic corporations should be taxed only on the amount of dividends received after taxes, in his budget speech on July 10, 2014. That discrepancy might be eliminated by following this advice. Consequently, the corporations had to do new DDT calculations, as seen in the diagram below:

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| | amount of dividend: DDT @ 15% of Rs. 588 = Rs. 88 approximately + Surchage and Cess, as applicable |
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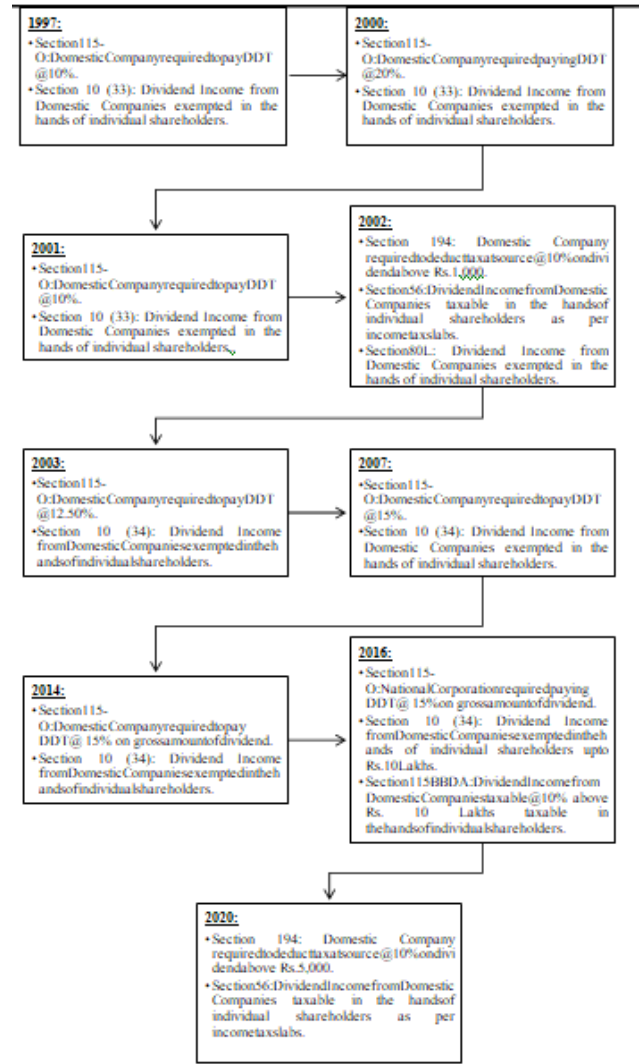
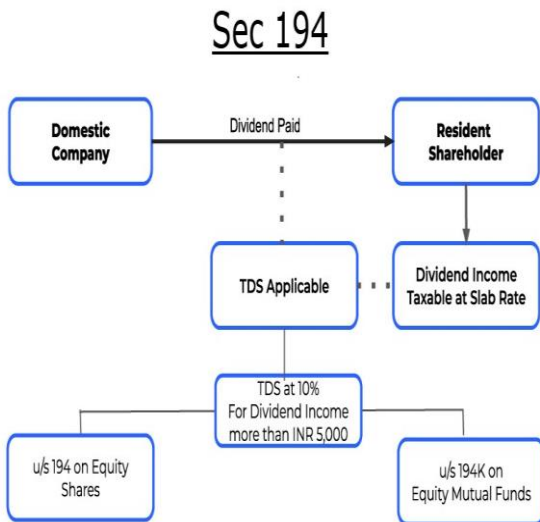
2016: Tax on certain dividends received from domestic corporations was added to the Income Tax Act, 1961, in the Finance Act, 2016 w.e.f. April 1, 2017. In his budget address on February 29, 2016, then-Honourable Finance Minister Shri Arun Jaitley said that the current system of taxes on dividends applied consistently to all investors, regardless of their income and the tax rates applicable to them. This resulted in a distortion of the tax system's fairness and progressivity. He went on to say that those with substantially higher incomes might shoulder a greater portion of the tax burden.

Those shareholders who received dividends totaling more than Rs. 10 lakhs in a financial year from domestic enterprises were now compelled to pay a 10% income tax on the excess payouts.

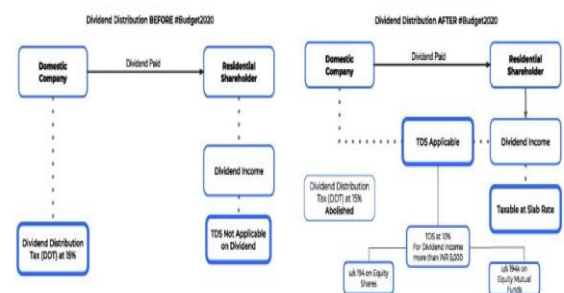
2020: Honourable Finance Minister, Shrimati Nirmala Sitharaman's budget address on February 1, 2020, said that DDT raised the tax burden on those in lower tax bands. She also claimed that international investors' returns on equities in India were lowered since they couldn't claim credit for DDT in their home countries. As a result, she suggested deleting this provision and implementing taxation of dividends as a percentage of shareholders' tax rates, which would boost the attractiveness of the stock market in India and give some relief to a large majority of investors. According to Section 194 of the 1961 Income Tax Act, dividends will once again be taxed and deducted for tax purposes, as mentioned in her budget address. It has been restored to its previous status under the terms of Section 194 of the Income Tax Act, 1961, and the firms must now deduct tax at source on dividends at a rate of 10 percent as per the rules of The Finance Act, 2020 as of April 1, 2020 as per Dr. MADIREDDI SSV SRIKUMAR. MCOM, MBA, PHD. Associate Professor Vision P.G. College and Dr Naveen Prasadula. MSC (I.T), MBA, PHD (2020)

| Pre Amendment:- | Post Amendment:- |
|---|--|
| Dividend Declared=Rs. 500 | Dividend Declared=Rs. 500 |
| DDT Computation: - DDT@15%of Rs.500=Rs.75+Surchageand Cess,as applicable | DDT Computation: - NowRs.500 is considered as the amount of dividend net of taxes, meaning there by, amount of dividend after deducting DDT @ 15%. Hence, Rs. 500 is the amount at 85%. DDT of 15% has to be applicable on the gross amount of dividend declared i.e.,100% and not the net amount i.e.,85%. Hence, the first step is to convert the amount of dividend net of taxes to gross amount: $Rs.500/(100-15\%)=Rs.588$ approximately Now, the second step is to compute DDT on this gross |

Department of Business Management Osmania University. However, if dividends are given in any form other than cash and the total amount of dividends to be paid to the shareholder does not exceed Rs. 5,000, no tax is needed to be deducted. From 1997 through 2020, the following flowchart depicts how dividends paid by domestic corporations to their individual equity owners would be taxed:



TAXABILITY OF DIVIDEND - DIVIDEND DISTRIBUTION TAX (DDT)



Taxes paid on dividends

Dividends paid out by corporations and mutual funds on or after April 1, 2020 will be subject to a TDS under the Finance Act, 2020. TDS is imposed at a rate of 10% on dividends received from a corporation or mutual fund that are more than Rs 5,000. Government cut TDS rate to 7.5% for distribution from May 14, 2020 to March 31, 2018,

however, in response to the COVID-19 crisis. When the person files their ITR, the tax savings will be used as a credit against their overall tax obligation. On June 15, 2020, and for example, Mr. Ravi got a dividend of Rs 6,000 from an Indian firm. A TDS @7.5 percent would be deducted from his dividend income of Rs 450 since his dividend income is more than Rs 5,000. Mr. Ravi will get Rs 5,550 in the form of a check. In addition, Mr Ravi must pay tax on the dividend income at the slab rates in effect for FY 2019-20. (AY 2019-20). Only those who are not residents of the United States are obligated to deduct 20 percent TDS (tax deducted at source) from their taxable income. The non-resident must provide documentation such as Form 10F, a declaration of beneficial ownership, a certificate of tax residency, etc. in order to take advantage of the reduced deduction owing to a favourable treaty rate with the nation of residence. In the absence of certain papers, a larger TDS would be deducted, which may be claimed when submitting an ITR.

RESEARCH AND METHODOLOGY

Data and Sources of Data:

On the basis of secondary data gathered from the 1961 Income Tax Act, Union Budget Speeches by Honourable Finance Ministers, and annual finance acts from time-to-time, this analysis has been based.

Tools and Techniques:

Qualitative research was employed in this study, which relied only on the reading of relevant legislation and documents for data collection.

Subtracting the cost of dividends from your income:

The Finance Act, 2020 also allows for interest expenses spent on dividends to be deducted from income. Dividends should not be deducted at a rate of more than 20%. A deduction for commission or salary expenses made in order to generate dividend income is not allowed. A maximum of Rs 1,200 of interest paid by Mr Ravi on a loan to invest in equity shares during FY 2019-20 is permissible in this case.

COMMENTARY

The economic double taxation that continues when dividends are taxed must be considered. To put it another way, dividend is nothing more than a firm handing out its earnings to its shareholders. To what end are we levying a tax on the transfer of profits? Even with partnership businesses, the earnings are divided among the partners. As a result, a partner's portion in the partnership firm's earnings is exempt

under section 10 (2A) of the Income Tax Act, 1961, since it has already been taxed by the partnership business. Corporate earnings are distributed to shareholders in the same way. In the hands of businesses, these earnings have already been taxed. Why, therefore, is it necessary for firms or dividend recipients to pay tax on their dividends. Currently, the same amount is taxed twice by levying taxes with different names, as the corporation pays corporate tax on its profits and the shareholder pays income tax on its dividend income, since the recipient shareholder is obligated to pay tax on dividend according to his or her income tax slab. Even exacerbated by the presence of Section 115BBDA, the same sum was taxed twice as the corporations paid taxes on their earnings, DDT had to be paid by them, and shareholders with dividend income exceeding Rs. 10 lakhs had to pay income tax on such income. Even if the current government wanted to protect lower-income taxpayers from the increased DDT tax on dividend income, as Finance Minister Shrimati Nirmala Sitharaman stated in her budget speech on February 1, 2020, they should have exempted dividend income in the hands of such shareholders because it leads to economic double taxation in the first place.. A reduction in corporate tax rates should not be compensated for by increasing the burden on individual taxpayers.

CONCLUSION

It is apparent that dividend taxation has been like a roller coaster ride based on the numerous regulations that have been applicable. A major factor is the transition in taxes from conventional to indirect, then back again.. What a joke of the taxation system is it that the recipient shareholders had to pay tax on dividends, while enterprises had to pay tax on dividends, at the same time? This was a result of a lack of planning by the administration, or an experiment to see which method worked best.

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