

BA Part 2 (Paper - 4)

Economics (Hons)

Topic : **Direct Tax: Types, Advantages & Disadvantages**

### What is Direct tax?

In simple words, a direct tax is a tax that you directly pay to the authority imposing the tax. For instance, income tax is imposed by the government, and you pay it directly to the government. These taxes cannot be transferred to any other entity or person. There are several acts which govern direct taxes.

In India, CBDT (Central Board of Direct Taxes) which is governed by the Department of Revenue is responsible for the administration of direct taxes. The department is also involved in planning and providing inputs to the government regarding the implementation of direct taxes.

Common Types of Direct Taxes in India

Some of the most common types of direct tax implemented in India are as follows-

#### 1. Income Tax

The most common type of direct tax in India is income tax. It is imposed on the income you earn in a financial year based on the income tax slabs of the IT department. The tax is paid by individuals as well as businesses directly to the IT department. For individual taxpayers, there are also several tax deductions available under various sections of the IT Act.

#### 2. Securities Transaction Tax

If you are involved in stock trading, each of your trade also has a small constituent known as the securities transaction tax. Irrespective of whether you made money on the trade or not, you will have to pay this tax. The broker collects this tax from you and passes on to the securities exchange, which then pays it to the government.

#### 3. Capital Gains Tax

Every time you make capital gains, you will be required to pay capital gains tax. This capital gain could come from the sale of a property or from investments. Based on the capital gains and the duration for which you held the investment, you will be required to pay either LTCG (Long-Term Capital Gains) tax or STCG (Short-Term Capital Gains) tax.

## Benefits of Direct Taxes

There are some key benefits of direct taxes such as-

**Curbs Inflation-** In case if there is monetary inflation, the government can increase direct tax rates so that the goods and services demand can be reduced. As the demand falls, it helps in condensing inflation.

**Equitable-** Direct taxes are also known to be equitable as the progression principle is at its foundation. People with lower income pay lower taxes, and people with higher income pay higher taxes.

**Reduces Inequalities-** The higher taxes collected from the rich are used by the government to launch newer initiatives for the poor. The initiatives provide income sources to people with lower income, helping them improve their living standards.

## Disadvantages of Direct Taxes

Direct taxes also have some drawbacks such as

**Considered a Burden-** As taxpayers are required to pay direct taxes like income tax in a single lump sum every year, they are considered a burden. Moreover, even the documentation process is generally complex and time-consuming.

**Evasion is Possible-** While the government has made tax evasion very difficult now, there are still many fraudulent practices through which individuals and businesses can avoid or pay lower taxes than they should.

**Restrains Investments-** Due to the imposition of direct taxes like securities transaction tax and capital gains tax, a lot of people avoid investing. So, in a way, direct taxes restrain investments.

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