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B.Com Honours | Semester VI | Calicut University

CORPORATE TAXATION AND TAX PLANNING

Course Code: COM6EJ313 • Module 4 Notes

Module IV: Corporate Tax Planning in Managerial Decisions

Covers tax planning in capital structure (Debt vs Equity), dividend policy, bonus shares, capital gains, Owning vs Leasing, Make vs Buy, Repair vs Replace, Export vs Domestic, & Shut Down decisions.

Unit 14: Tax Planning for Specific Management Decisions

Decision Matrix: Evaluating tax consequences of alternative financial & operational choices before execution.

Unit 15: Tax Planning in Capital Structure (Debt vs Equity)

Debt Tax Shield: Interest paid on debentures/loans is a fully deductible tax expense under Sec 36(1)(iii), creating a tax shield ($\text{Tax Shield} = I \times t$). Dividend paid on equity is an appropriation of profit (non-deductible).

Unit 16: Tax Planning with Dividend Policy & Bonus Shares

Bonus Shares & Dividends: Issue of bonus shares is not taxable in hands of shareholders upon allotment; tax applies only when sold as capital gains.

Unit 17: Tax Planning with Investments & Capital Gains

Capital Gains Planning: Utilizing Sec 54EC bonds or Sec 54G (shifting industrial undertaking from urban area) exemptions.

Unit 18: Tax Planning in Owning vs Leasing & Make vs Buy

Lease vs Buy: Lease rent is fully deductible tax expense; buying allows depreciation (Sec 32) & interest deduction.

Unit 19: Export vs Domestic & Shut Down Decisions

Export Incentives: Deductions under Sec 10AA for SEZ export units; tax impact of temporary shut down vs continuation.

Practical Solved Tax Shield Problem (Capital Structure Debt vs Equity Financial Advantage): A company requires $₹50,00,000$ capital. Tax Rate = 30%. Compare Earning After Tax (EAT) under two plans:
- **Plan A (Equity):** 100% Equity Shares ($₹50,00,000$).
- **Plan B (Debt):** 50% Equity ($₹25,00,000$) & 50% Debentures ($₹25,00,000 @ 12\%$ Interest). EBIT = $₹15,00,000$.

Debt Tax Shield = Debt Interest * Corporate Tax Rate = (₹25,00,000 * 12%) * 30% = ₹90,000

Step-by-Step Capital Structure Tax Shield Working:
1. **Plan A (Equity):** EBIT = $ ₹15,00,000 $. Interest = $ ₹0 $. Tax @ 30% = $ ₹4,50,000 $. **EAT = ₹10,50,000**.
2. **Plan B (Debt):** EBIT = $ ₹15,00,000 $. Interest ($ 12\% \text{ of } ₹25,00,000 $) = $ ₹3,00,000 $. Taxable Profit = $ ₹12,00,000 $. Tax @ 30% = $ ₹3,60,000 $. **EAT = ₹8,40,000**.
3. **Tax Savings on Debt (Tax Shield):** Tax in Plan A (₹4,50,000) - Tax in Plan B (₹3,60,000) = $ \mathbf{₹90,000} $.

Practical Case Framework 2 (Owning vs Leasing Asset Financial & Tax Evaluation Matrix): Compare asset decision, tax benefit deductible, capital outlay, and net cash outflow impact.

Owning vs Leasing Tax Evaluation Table:

Asset Decision Option	Tax Deductible Expenses Available	Financial & Tax Outflow Advantage
Owning Asset (Buy)	Depreciation (Sec 32) + Loan Interest (Sec 36)	Higher initial capital outlay; long-term asset value
Leasing Asset (Lease)	100% Lease Rental paid is tax deductible	Preserves capital liquidity; 100% tax write-off