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THE TREND AND PATTERN OF INCOME TAXATION IN INDIA

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Abstract
The Income Tax department in India is responsible for policy formulation and planning for direct taxes and for administering direct tax laws like the Income-tax Act, Wealth-tax Act and various Finance Acts passed during every budget session. Today it is the biggest revenue mobiliser for the government. Direct tax collections had seen tremendous growth due to policy innovations, rationalization of tax structure, improvement in tax administration and tax payer's services through intensive use of technology. The economic crisis of 1991 led to structural tax reforms in India with main purpose of correcting the fiscal imbalance. In India steps are taken to improve the tax-GDP ratio by augmenting tax collections by improving tax administration by leveraging technology and facilitating public interface, where required, through appropriate training and capacity building. This article discusses on origin and evolution of Income Tax, income tax structure, expenditure incurred by the Indian government to collect taxes and direct tax GDP ratio. The Direct Tax Collection as a percentage of GDP is doubled as a result of improved tax administration and better tax compliance.

Key Words: Evolution, GDP Ratio,Income Tax, Revenue, Tax Rate, Tax Collection.

Introduction

Only two things are certain in this life – death and taxes
-Mark Twain

Income tax is a key source of funds that any government uses to finance its activities and serve the public. It has been aptly said that taxes are the price we pay for civilization. No civil society is possible without revenue. One of the most important sovereign functions of any government is the collection of tax for development, security and governance. Taxation plays a critical and pivotal role in the process of advancement and growth of any country. Objectives of the tax policy of any country are akin to its general economic policy. Taxes constitute major source of revenue for the government. A sound tax system is vital for development of public finance of any country. The Income Tax Act 1961 has become very complex and virtually unintelligible to the common man by virtue of a complicated structure, numerous amendments, frequent policy changes and a multitude of judgments that gave varying interpretations to already undecipherable provisions. The Direct Tax amendments of the financial year, 2012-13 replaced the five decade old Income tax Act, 1961 to make the Indian tax structure straightforward.

Origin and Evolution of Income Tax in India

Ancient Period

There is enough evidence to show that taxes on income in some form or the other were levied even in primitive and ancient communities. References to taxes in ancient India are found in "Manusmriti" and "Kautilya‟s Arthashastra". Manu the ancient sage and law giver stated that the Kings were to be levied taxes according to Sastras. He advised that taxes should be related to income and should not be excessive. He laid down that traders and artisans should pay 1/5th of their profits in gold and silver, while the agriculturists were to pay 1/6th , 1/8th and 1/10th of their produce depending upon their circumstances. The Manu Sastra analysis clearly shows the existence of a well-planned taxation system, even in ancient times.

Initial Period (1860-1886)

Income tax in its modern form was introduced in India for first time in 1860 by the British Government to overcome the financial crisis following the events of 1857. Initially Government introduced it as a temporary

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measure of raising revenue under the Income Tax Act 1860 for a period of five years. Different tax rates were prescribed for different heads of income. In the year 1867, it was transformed as license tax on trade and profession. In the year 1869, the license tax was replaced by Income Tax again. The assessments were made on arbitrary basis leading to inequality, unpopularity and widespread tax evasion. Income Tax was withdrawn in the year 1874. After the great famine of 1876-78, the Government introduced local Acts for income tax in different provinces. With several amendments these Acts remained in force till 1886. Thus, the period from 1860 to 1886 was a period of experiments in the context of income tax in India.

Pre Independence Period (1886-1947)

In 1886, a new Income Tax Act was passed with great improvements than the previous Acts. This Act with several amendments in different years continued till 1918. In 1918, a new Act was passed rescinding all the previous Acts. For the first time, this Act introduced the concept of aggregating income under different heads for charging tax. In 1921, the Government constituted “All India Income Tax Committee” and on the basis of recommendation of this committee a new Act (Act XI of 1922) was enacted. This Act is a landmark in the history of Indian Income Tax system. This Act made income tax a central subject by shifting the tax administration from the Provincial Governments to the Central Government. During this period the Board of Revenue (Central Board of Revenue) and Income Tax Department with defined administrative structure came into existence.

Post-Independence Period

The Income Tax Act 1922 continued to be applicable to independent India. During the early post-independence period, the Income Tax legislation had become very complicated on account of innumerable changes. During this period tax evasion was wide spread and tax collection was very expensive. In 1956, the Government of India referred the Act to a Law Commission to make the Income Tax Act simpler, logical and revenue oriented. The income-tax was introduced in India for the first time in 1860 by British rulers following the mutiny of 1857. The period between 1860 to 1886 was a period of experiments in the context of income-tax. This period ended in 1886 when first Income tax Act came into existence. The pattern laid down in it for levying of tax continues to operate even to-day though in some change form. In 1918 another Act – Income-tax Act, 1918 was passed nut it was short lived and was replaced by Income tax Act, 1922 and it remained in existence and operation till 31st March, 1961.

Tax Reforms in Globalized Era

The economic crisis of 1991 led to structural tax reforms in India with main purpose of correcting the fiscal imbalance. Subsequently, the Tax Reforms Committee headed by Raja Chelliah (Government of India, 1992) and Task Force on Direct Taxes headed by Vijay Kelkar (Government of India, 2002) made several proposals for improving Income Tax System. These recommendations have been implemented by the government in phases from time to time. As regarding the personal income tax, the maximum marginal rate has been drastically reduced, tax slabs have been restructured with low tax rates and exemption limit has been raised. In addition to this, government rationalized various incentive provisions and widened TDS scope. In case of corporate tax, the government has reduced rates applicable to both domestic and foreign companies, introduced depreciation on intangible assets and rationalized various incentive provisions. Some new taxes have been introduced such as Minimum Alternative Tax and Dividend Distribution Tax, Securities Transaction Tax, Fringe Benefit Tax and Banking Cash Transaction Tax. In India the foundation for the Tax Reforms were laid down in 1991 itself when the economy was liberalized .After reforms, tax rates have been rationalized and tax laws have been simplified resulting in better compliance, ease of tax payment and better enforcement.

E Governance Initiatives

The e-filing project is an eminent e-governance and e-delivery measure taken by the Income Tax Department for better services to the taxpayers and was notified in 2006-2007. During the Financial Year 2012-13, the e-filing website has been revamped and made live on 9th November, 2012 with many new utilities like extension of electronic filing of all other forms as prescribed in the I-T Rules 1962, enabling access to history of returns filed, and other Services in the e-filing website.

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The project is aimed at enabling E-filing of Income tax returns, Audit Reports and other forms of the Income Tax over Internet directly by taxpayers and through e-return intermediaries (ERIs) on Virtual Private Networks, enabling e-filing of Income Tax Returns and other web enabled services using XML to enable public private participation in the filing of returns. The income tax department has taken up a new role as an assessee-friendly facilitator with a portal https://incometaxindiaefiling.gov.in is functional with a host of services to taxpayers. The new system also offers personalized services including pre-filling of returns with assesssee details and 26AS data; online and offline filing of returns etc. The system includes submission of online rectifications, verification of status updates for receipt of ITR-V, processing status and refunds for e-filed returns processed at CPC, Bangaluru. Select information is also available through a mobile interface.

Direct and Indirect Tax

Direct Taxes are the taxes that are levied on the income of individuals or organizations. Income tax, corporate tax, inheritance tax are some instances of direct taxation. Income tax is the tax levied on individual income from various sources like salaries, investments, interest etc. Corporate tax is the tax paid by companies or firms on the incomes they earn. Indirect taxes are those paid by consumers when they buy goods and services. These include excise and customs duties. Customs duty is the charge levied when goods are imported into the country, and is paid by the importer or exporter. Excise duty is a levy paid by the manufacturer on items manufactured within the country. Usually, these charges are passed on to the consumer. The following table 1 depicts the revenue generated by Central and State government through Direct and Indirect taxes.

Table 1:Direct and Indirect Tax Revenues of Central and State Governments

Year	Centre (gross) Direct Revenue	Centre (gross) Indirect Revenue	States Direct Taxes	States Indirect Taxes	Tax Revenues
	(In Billion Rupees)				
2000-2001	683.06	1200.46	128.57	997.69	3009.72
2001-2002	691.97	1171.77	156.79	1068.94	3089.47
2002-2003	830.85	1315.81	172.17	1201.35	3520.18
2003-2004	1050.90	1476.58	202.13	1351.38	4080.99
2004-2005	1328.47	1705.46	239.81	1580.01	4853.75
2005-2006	1652.49	1993.98	301.79	1817.68	5765.94
2006-2007	2302.49	2412.63	388.29	2136.82	7240.23
2007-2008	3122.43	2791.04	434.46	2427.03	8774.96
2008-2009	3338.54	2696.45	441.32	2786.73	9263.04
2009-2010	3774.87	2438.81	473.87	3158.56	9846.11
2010-2011	4459.94	3431.78	627.25	3981.70	12500.67
2011-2012	5006.51	3970.15	764.02	4793.77	14534.45
2012-2013	5702.57	5027.34	902.55	5550.81	17183.27

Source: Ministry of Finance

The above table 1 reveals that an amount of 17183.27 Billon total tax revenue was generated during FY 2012-13. The Central government collected total direct tax revenue as ₹.5702.57 billion and indirect tax revenue to the tune of ₹.5027.34 billion during the FY 2012-13. The State government collected as total direct tax revenue as 902.55 billion and indirect tax revenue as ₹5550.81 billion during FY 2012-13.

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Income Tax Structure in India

The tax system in India mainly, is a three tier system which is based between the Central government, State Governments and the Local government organizations. India has a well-developed tax structure with clearly separated authority between Central and State Governments and local bodies. The primary objective of any tax law and its administration is to raise revenue for the purpose of funding Government expenditure. The amount of revenue raised is primarily dependent upon the collective tax base and the effective tax rates. Tax rate structure is the main component of tax policy of any country. It affects tax base and tax compliance to a large extent. It is believed that lower tax rates lead to higher compliance and vice versa. In our country there are different tax rates for different persons. With reference to tax structure, in 1860 when the systematic taxation on income was first introduced in India the tax rate was only 2 per cent on income between ₹ 200 to ₹.500 and it was 4 per cent on income above ₹ 500. Upto Rs.2,000 and a standard rate of 5 pies per rupee was applicable to all income above ₹.2,OOO. But, in 1916 the principle of gradation came into force and for incomes in different brackets, different rates of tax were prescribed. A super tax was also imposed in 1917. In 1950-51 the tax rate was 9 pies for income from ₹.1,500 to Rs.5,000 and it was 4 annas beyond ₹. 15,000. The Marginal tax rate worked out from a minimum of 4.69 per cent to a maximum of 25 per cent. A super tax was imposed beyond ₹ 25,000 that ranged from 3 annas to 8 annas and 6 pies per rupee.The following table shows the income tax structure in India from the period 1949-50 to 2012-13.

Table 2: Evolution of Income Tax Rate Structure in India

Year	Exemption Limit	Number of Rates	Entry Rate	Peak Rate	Income at which Peak Rate Applies
1949-1950	1500	4	4.69	25.00	15000
1955-1956	2000	5	4.93	26.25	15000
1960-1961	3000	7	3.15	26.25	20000
1970-1974	5000	11	11.00	93.50	200000
1974-1975	6000	8	13.20	77.00	70000
1980-1981	8000	8	15.00	66.00	100000
1985-1986	18000	4	25.00	50.00	100000
1990-1992	22000	4	20.00	56.00	100000
1995-1998	40000	3	20.00	40.00	120000
1998-1999	50000	3	10.00	30.00	150000
1999-2000	50000	3	10.00	33.00	150000
2000-2001	50000	3	10.00	35.10	150000
2001-2002	50000	3	10.00	30.60	150000
2002-2003	50000	3	10.00	31.50	150000
2003-2004	50000	3	10.00	33.00	150000
2004-2005	50000	3	10.00	33.66	150000
2005-2007	100000	3	10.00	33.66	250000
2007-2008	110000	3	10.00	33.99	250000
2008-2009	150000	3	10.00	33.99	500000
2009-2010	160000	3	10.00	30.90	500000
2010-2011	160000	3	10.00	30.90	800000
2011-2012	180000	3	10.00	30.90	800000
2012-2013	200000	3	10.00	30.90	1000000

Source: Indiastat

The above table clearly reveals that the exemption limit of Rs 1500 in 1949-50 kept rising to Rs. 50,000 upto 1998-98 and remained unaltered at ₹. 50000 until 2004-05.The exemption limit begin to raise again from the year 2005-06 to 2012-13 and increased from ₹. 1,00,000 to ₹. 2,00,000. The number of tax rates reduced from 11 in

1974 to 8 in 1992 and thereafter it was 3 till 2013.The peak rate was found highest in the years 1970-73 with 93.50. The buoyancy in personal income tax collection shows that the rationalization of the slabs and moderation in tax rates aid in improving tax collection. Tax base is a crucial factor affecting the tax revenue. It is a matter of serious concern that tax base is very narrow in our country. In a population of more than 100 crore there are around 340 lakh income taxpayers i.e. only 3.4 per cent are covered under the tax net. So, there is a need to broaden tax base.

Cost of Collection of Direct Taxes

One of the achievements for which the Income-Tax (I-T) department takes considerable credit is the low cost of collecting income-tax. In the pre-assessment stage collections, the costs are incurred by the assessees and not by the Department. In the case of corporate assessees, around 80 per cent of gross collections are made at the pre-assessment stage, of which advance tax accounted for more than 50 per cent. In the case of non-corporate assessees, 90 per cent of the gross collections are made at pre-assessment stage, with TDS making up around 52 per cent of this.For pre-assessment stage collections; the I-T Department does not incur any expenditure, except a miniscule amount for processing the payments. Hence a major part of costs are incurred during post assessment stage.

Table 3:Total collction of direct taxes and expenditure incurred for collection

Financial Year	Total collections	Total Expenditure	Exp. as % of collection
1998-1999	46,600	852	1.83%
1999-2000	57,959	894	1.54%
2000-2001	68,305	929	1.36%
2001-2002	69,198	933	1.35%
2002-2003	83,088	984	1.18%
2003-2004	105,088	1050	1.00%
2004-2005	132,771	1138	0.86%
2005-2006	165,208	1194	0.72%
2006-2007	230,181	1348	0.59%
2007-2008	312,213	1687	0.54%
2008-2009	333,828	2286	0.68%
2009-2010	378,063	2726	0.72%
2010-2011	446,935	2698	0.64%
2011-2012	4,94,799	2579	0.60%
2012- 2013	**5,82,000**	3492	0.60%

Source: Ministry of Finance

Total cost of direct tax collection showed a decreasing trend from 1.83% in 1998- 1999 to 0.54 per cent in 2007-08. In 2008- 09, the costs rose because of deceleration in tax collection and increase in establishment cost. As a result of improved tax administration and better tax compliance direct tax collection is displaying positive trends. An amount of 4,94,799 crore has been collected up to 31 March, 2012 at a of around 10.71% over previous year's corresponding collection of ‘ growth rate 446,935 crore. During the span of last ten years, the collection has increased by five times . During 1998-1999, the direct taxes collection was ` just 46600 crores and for the year 2012-2013, the direct taxes collection has reached ` 5,82,000 crore. The performance on the Direct Taxes front is commendable considering the fact that the cost of collection has decreased from 1.36% in the year 2000-2001 to 0.60% in 2011-2012 being one of the lowest in the world i.e the Department spends only 60 paisa for each 100 rupees collected.

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Direct Tax GDP Ratio

Tax-GDP ratio has been widely recognized as a useful indicator of development of a nation. As per certain estimates, a minimum of 18 percent of its value may be required in most of the developing countries (including India). India is believed to have lower tax GDP ratio. As per World Bank Database (Taxes collected by Central Government) the 9.7 % ratio in case of India , during 2010, is less than the world average of 14.2 % and much lower than 19.3 % ratio in case of European Union , which has traditionally higher levels of Tax GDP Ratio. Some argue that higher tax GDP ratio translates into better infrastructure etc by taxing the rich through direct taxes but in the globalised world things have become increasingly complex. Increasing corporate taxes could have repercussions through business moving elsewhere. India currently raises only 15.5 per cent of its GDP as tax revenues, making it one of the lowest taxes of all G20 countries. By comparison, the average tax to GDP (gross domestic product) ratio in OECD (Organisation for Economic Cooperation and Development) countries is almost 10 percentage points higher at 24.6 per cent.

Table 4 : Direct Tax GDP Ratio

(₹ in crore)

Financial year	Net collection of direct taxes	(in crore)	Direct tax GDP ratio	GDP growth rate%	Tax growth rate %	Buoyancy factor (%)
2002-03	83088	2458084	3.38%	7.76%	20.07%	2.59
2003-04	105088	2754621	3.81%	12.06%	26.48%	2.19
2004-05	132771	3242209	4.10%	17.70%	26.34%	1.49
2005-06	165216	3693369	4.47%	13.92%	24.44%	1.76
2006-07	230181	4294706	5.36%	16.28%	39.32%	2.42
2007-08	312213	4987090	6.26%	16.12%	35.64%	2.21
2008-09	333818	5630063	5.93%	12.89%	6.92%	0.54
2009-10	378063	6457352	5.85%	14.69%	13.25%	0.9
2010-11	446935	7674148	5.82%	18.84%	18.22%	0.97
2011-12	494799	8855797	5.59%	15.40%	10.71%	0.7

(Source : Pr CCA CBDT and Economic Survey 2012-13/CSOI)

Revenue collection from Direct Taxes has been growing consistently for the last five years. The Direct Tax Collections as a percentage of GDP has grown from 2.68% in F.Y. 1998- 99 to 6.21% in F.Y. 2008-09.As a result of improved tax administration and better tax compliance direct tax collection is displaying positive trends An amount of Rs.3,37,150 crore (provisional) has been collected up to 31st March'09 at a growth rate of around 8% over previous year's corresponding collection of ₹.3,12,202 crore. During the span of last five years, the collection has more than trebled. During 2003-04, the direct taxes collection was ₹.1,05,088 crore and for the year 2008-09, the direct taxes collection has reached ₹.3,37,150 crore (provisional). The collection from TDS till 31st March, 2009 is ₹.1,33,500 crore which is at a very healthy growth rate of 25% over corresponding figure last year.

Revenue collection from Direct Taxes has been growing consistently. An amount of ₹. 4,94,799 crore (Provisional) was collected during FY 2011-12 at a growth rate of around 10.71% over previous year's corresponding collection of ₹ 4,46,935 crore. The performance on the Direct Taxes front is commendable considering the fact that the cost of collection has decreased from 1.36% in the FY 2000-2001 to 0.60% during FY 2011-12 being one of the lowest in the world i.e. the Department spends only 60 paisa for each 100 rupees collected. Revenue collection from Direct Taxes has been growing consistently or the last five years. The Direct Tax Collections as a percentage of GDP has grown from 2.68% in F.Y. 1998-1999 to 5.67% in F.Y. 2010-2011. This has been made possible largely due to the revamping of the TDS administration and the reach out programmes through training and educating the senior management and D.D.Os of other departments and PSUs.

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The performance on the Direct Taxes front is commendable considering the fact that the cost of collection has decreased from 1.44% in the year 2001-02 to 0.53% in 2008-09 being one of the lowest in the world. With Direct Tax share of 37.7 % in total taxes, India's tax structure is perceived to be regressive. Even developing countries like South Africa (57.5 %), Indonesia (55.85 %) and Russia (41.3 %) have a more progressive tax structure, in terms of the contribution of Direct Taxes to total tax revenue. All developed countries that are part of the G20 have greater share of Direct Taxes in their total taxes than India, with figures as high as 75.8 % for USA

Conclusion

Indian tax administration is not easy. Economists suggest the government to toe the global tax rate line which it has done historically. Tax rates in India were more than 90 per cent in the early 1970s when Britain's rate varied between 75 and 90 per cent. The US pegged taxes at 90 per cent in the 1960s. Today, India taxes income at three rates - 10 per cent, 20 per cent and 30 per cent . Direct taxes can be increased by taxing the rich more, increasing the share of property tax and re-introducing of inheritance tax. Overall the tax effort is very low. We need to raise it from 15 per cent to at least 20 per cent. Other countries rely more on direct taxation, which raises greater revenues from those who can afford to pay more and therefore have a more progressive structure of taxation than India. India raises only 15.5 per cent of GDP as tax revenues- the lowest taxes of all G20 nations, while the average tax-GDP ratio in OECD countries is at 24.6 per cent. India should mobilize tax revenue and rely more on direct taxes instead of indirect taxes, which are regressive because it affects the rich and poor alike.

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