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AN IMPACT OF 'INCOME TAX'

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ABSTRACT

Income Tax is a main source of revenue to the government. Income Tax is necessary for equal distribution of income and wealth in the economy. It stresses on income equality. We know that income tax is progressive in nature that is higher rate of tax on higher earnings. Government collect the income tax from individuals and companies who have higher earnings and spend that tax revenue on poor people in the form of subsidies, concessions, health, education etc. as public expenditure. Recently the Advisor to the Governor K.K. Sharma said that "Taxation necessary for egalitarian, developed society." The Advisor said it is important that people pay their taxes on time as the same gets used for various developmental works which include constructions of schools, colleges, hospitals, bridges, macadamizing of roads and other like things. The Advisor said that the concept of taxation finds its root in our historical texts also and it has been used as a means for bringing a balance in the society so that equitable development of the society takes place and people enjoy the benefits of development. He said that the people by regularly filling their income tax returns are contributing their bit in building a strong and prosperous nation.

INTRODUCTION

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 rationalised 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 rationalised various 6 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. However, Fringe Benefit Tax and Banking Cash Transaction Tax were withdrawn by Finance Act, 2009. The Income tax administration was restructured with effect from August 1, 2001 to facilitate the introduction of computer technology. Further, keeping in mind the global developments, the department has made considerable efforts for reforming the tax administration in recent years. Some important measures in this direction are introduction of mandatory quoting of Permanent Account Number (PAN), e-filing of returns, e-TDS, e-payment, Tax Information Network (TIN), Annual Information Return (AIR) for high value transaction, Integrated Taxpayer Profiling System (ITPS), Refund Banker Scheme in certain cities etc. The main objective of these reforms has been to enhance tax revenue by expanding the taxpayer base, improving operational efficiency of the tax administration, encouraging voluntary tax compliance, creating a taxpayer friendly atmosphere and simplifying procedural rules.

Keywords: Origin and Evolution of Income Tax in India, Concept of Income Tax, Major defects in the tax structure of India, Data Analysis, Tax evasion V/s. tax avoidance, Tax Evasion and black money, etc.

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 king should levy 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 detailed analysis given by Manu on the subject clearly shows the existence of a well planned taxation system, even in ancient times. Kautilya's Arthasastra was the first authoritative text on public finance, administration and the fiscal laws. Collection of income tax was well organized during Mauryan Empire. Schedule of tax payment, time of payment, manner and quantity were fixed according to Arthasastra. It is remarkable that the present day system of taxation is in many ways similar to the system of taxation given by Kautilya 2300 years ago.

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 measure of 3 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 licence tax on trade and profession. In the year 1869, the licence 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 repealing 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 Law Commission submitted its report in September 1958 and in the meantime the Govt. also appointed a Direct Taxes Administration Enquiry Committee to suggest the measures for minimizing the inconvenience to the assessees and prevention of tax evasion. This committee submitted its report in 1959. The recommendations of the Law Commission and the Enquiry Committee were examined and extensive tax reform programme was undertaken by the Government of India under the supervision of Prof. Nicholas Kaldor. The Income Tax Bill 1961, prepared on the basis of the Committee's recommendations and suggestions from Chamber of Commerce, was introduced in the Lok Sabha on 24.4.1961. It was passed in September 1961 by Lok Sabha. The Income Tax Act 1961 came into force on April 1, 1962. It applies to whole of India including the state of Jammu and Kashmir. It is a comprehensive piece of legislation having 23 Chapters, 298 Sections, various sub sections and 14 schedules. Since 1962, it has been subjected to numerous amendments by the Finance Act of each year to cope with 5 changing scenario of India and its economy. Moreover the Central Board of Direct Taxes is empowered to amend rules and to clarify instructions as and when it becomes necessary. Besides this, amendments have also been made by various Amendment Acts e.g. Taxation Laws Amendment Act 1984, Direct Taxes Amendment Act 1987, Direct Taxes Law (Amendment) Acts of 1988 and 1989, Direct Taxes Law (Second Amendment) Act 1989 and at last the Taxation Law (Amendment) Act 1991. As a matter of fact, the Income Tax Act 1961 has been amended drastically. It has therefore become very complicated both for administration and taxpayers.

Concept of Income Tax

Let us begin by understanding the meaning of tax. Tax is a fee charged by a Government on a product, income or activity. There are two types of taxes - direct taxes and indirect taxes.

Direct Taxes: If tax is levied directly on the income or wealth of a person, then, it is a direct tax e.g. Income-tax.

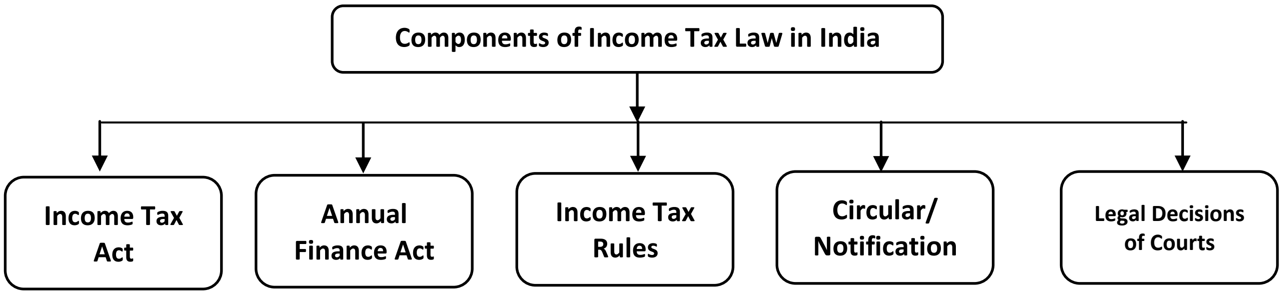
Indirect Taxes: If tax is levied on the price of a good or service, then, it is an indirect tax e.g. Goods and Services Tax (GST) or Custom Duty. In the case of indirect taxes, the person paying the tax passes on the incidence to another person.

Income Tax Act 1961 :

The levy of income-tax in India is governed by the Income-tax Act, 1961. In this book, we shall briefly refer to this as the Act.

• It came into force on 1st April, 1962.

• It contains 298 sections and XIV schedules.



Taxability of Income :

The incidence of tax on any assesse depends upon his residential status under the Act. For all purposes of income-tax, taxpayers are classified into three broad categories on the basis of their residential status viz.

(1) Resident and ordinarily resident

(2) Resident but not ordinarily resident

(3) Non-resident.

Residential Status and Scope of Total Income: Whether the following incomes are to be included in Total Income?

Scope of total Income	Ordinarily Resident	Not ordinarily Resident	Non Resident of India
Income received or deemed to be received in India during the previous year	Yes	Yes	Yes
Income accruing or arising or deeming to accrue or arise in India during the previous year	Yes	Yes	Yes
Income accruing or arising or deeming to accrue or arise in India during the previous year	Yes, even if such income is not received or brought into India during previous year	Yes, but only if such income is derived from a business controlled in or profession set up in India; Otherwise, No.	No

Computation of Total Income :

a. Determine the residential status

(Ordinarily Resident, Not Ordinarily Resident & Non Resident of India)

b. Classify income under five heads : 1)Salaries

2)Income from house property

3)Profits and gains from business or profession

4)Capital gains

5)Income from other sources

c. Compute income under each head applying the charging & deeming provisions and providing for permissible deductions/ exemptions thereunder.

d. Apply clubbing provisions

e. Set-off/carry forward and set-off of losses as per the provisions of the Act

f. Compute Gross Total Income (GTI)

g. Less: Deductions under chapter VI from GTI

h. Total Income (TI).

Steps to calculate tax:

Step 1 – Determination of residential status: The residential status of a person has to be determined to ascertain which income is to be included in computing the total income. The residential status as per the Income-tax Act, 1961 can be classified as under –(1) Resident and ordinarily resident

(2) Resident but not ordinarily resident

(3) Non-resident.

In the case of an individual, the duration for which he is present in India determines his residential status. Based on the time spent by him, he may be (a) resident and ordinarily resident, (b) resident but not ordinarily resident, or (c) non-resident.

The residential status of a person determines the taxability of the income. For e.g., income earned and received outside India will not be taxable in the hands of a non-resident but will be taxable in case of a resident and ordinarily resident.

Step 2 – Classification of income under different heads

The Act prescribes five heads of income. These are shown below –

1. Salaries: Salary, pension earned is taxable under the head "Salaries".

2. Income from house property: Rental income is taxable under the head "Income from house property".

3.Profits and gains from business or profession: Income derived from carrying on any business or profession is taxable under the head "Profits and gains from business or profession".

4.Capital gains: Profit from sale of a capital asset (like land) is taxable under the head "Capital Gains".

5. Income from other sources: The fifth head of income is the residuary head. The income which is not taxable under the first four heads will be taxed under the head "Income from other sources".

The tax payer has to classify the income earned under the relevant head of income.

Step 3– Computation of income under each head Income is to be computed in accordance with the provisions governing a particular head of income.

Exemptions: There are certain incomes which are wholly exempt from income-tax.

e.g. agricultural income. These incomes have to be excluded and will not form part of Gross Total Income. Also, some incomes are partially exempt from income-tax e.g. House Rent Allowance,

Education Allowance. These incomes are excluded only to the extent of the limits specified in the Act. The balance income over and above the prescribed exemption limits would enter computation of total income and have to be classified under the relevant head of income.

Deductions: There are deductions and allowances prescribed under each head of income. For example, while calculating income from house property, municipal taxes and interest on loan are allowed as deduction. Similarly, deductions and allowances are prescribed under other heads of income. These deductions etc. have to be considered before arriving at the net income chargeable under each head.

Step 4 – Clubbing of income of spouse, minor child etc.

In case of individuals, income-tax is levied on a slab system on the total income. The tax system is progressive i.e., as the income increases, the applicable rate of tax increases Some taxpayers in the higher income bracket have a tendency to divert some portion of their income to their spouse, minor child etc. to minimize their tax burden. In order to prevent such tax avoidance, clubbing provisions have been incorporated in the Act, under which income arising to certain persons (like spouse, minor child etc.) have to be included in the income of the person who has diverted his income for the purpose of computing tax liability.

Step 5 – Set-off or carry forward and set-off of losses

An assessee may have different sources of income under the same head of income. He may have profit from one source and loss from the other. For instance, an assessee may have profit from his textile business and loss from his printing business. This loss can be set-off against the profits of textile business to arrive at the net income chargeable under the head “Profits and gains of business or profession”. Similarly, an assessee can have loss under one head of income, say, Income from house property and profits under another heads of income, say, profits and gains of business or profession. There are provisions in the Income-tax Act, 1961 for allow in inter-head adjustment in certain cases.

However, there are also restrictions in certain cases, like business loss is not allowed to be set-off against salary income. Further, losses which cannot be set-off in the current year due to inadequacy of eligible profits can be carried forward for set-off in the subsequent years as per the provisions contained in the Act. Generally, brought forward losses under a particular head cannot be set-off against income under another head i.e., brought forward business loss cannot be set-off against income from house property of the current year.

Step 6 – Computation of Gross Total Income

The final figures of income or loss under each head of income, after allowing the deductions, allowances and other adjustments, are then aggregated, after giving effect to the provisions for clubbing of income and set-off and carry forward of losses, to arrive at the gross total income.

Step 7 – Deductions from Gross Total Income

There are deductions prescribed from Gross Total Income. These deductions are of four types –

1.DEDUCTIONS IN RESPECT OF CERTAIN PAYMENTS

Examples

1. Life Insurance Premium paid

2. Contribution to Provident Fund/Pension Fund

3. Medical insurance premium paid

4. Payment of interest on loan taken for higher education

5. Rent paid

6. Donation to certain funds, charitable institutions, etc.

7. Contributions to political parties

2. DEDUCTIONS IN RESPECT OF CERTAIN INCOMES

Examples

1. Employment of new employees

2. Royalty income etc. of authors of certain books other than text books

3. Royalty on patents

3. DEDUCTIONS IN RESPECT OF OTHER INCOME

Examples

1. Interest on deposits in saving account

2. Interest on deposits in case of senior citizens

4. OTHER DEDUCTIONS

Example :Deduction in case of a person with disability

Step 8 – Total income

The income arrived at, after claiming the above deductions from the Gross Total Income is known as the Total Income. It should be rounded off to the nearest multiple of ` 10.

Step 9 – Application of the rates of tax on the total income

The rates of tax for the different classes of assessee are prescribed by the Annual Finance Act. For individuals, HUFs etc., there is a slab rate and basic exemption limit. At present, the basic exemption limit is ` 2,50,000 for individuals. This means that no tax is payable by individuals with total income of up to ` 2,50,000. Those individuals whose total income is more than ` 2,50,000 but less than ` 5,00,00 have to pay tax on their total income in excess of ` 2,50,000 @ 5% and so on. The highest rate is 30%, which is attracted in respect of income in excess of 10,00,000. The tax rates have to be applied on the total income to arrive at the income-tax liability.

*SOURCE: INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

Step 10 - Surcharge / Rebate under section 87A

Surcharge: Surcharge is an additional tax payable over and above the income-tax. Surcharge is levied as a percentage of income-tax. In case where the total income of an individual/HUF/AOP/BOI exceeds ` 50 lakhs but does not exceed ` 1 crore, surcharge is payable at the rate of 10% of income-tax and in case total income exceeds ` 1 crore, surcharge is payable at the rate of 15% of income-tax.

Rebate under section 87A: In order to provide tax relief to the individual tax payers who are in the 5% tax slab, section 87A provides a rebate from the tax payable by an assessee, being an individual resident in India, whose total income does not exceed` 3,50,000. The rebate shall be equal to the amount of income-tax payable on the total income for any assessment year or an amount of ` 2,500, whichever is less.

Step 11 – Health and education cess on income-tax

The income-tax, as increased by the surcharge or as reduced by the rebate under section 87A, if applicable, is to be further increased by an additional surcharge called health and education cess on income-tax @4% of income-tax plus surcharge, if applicable.

Step 12 – Advance tax and tax deducted at source

Although the tax liability of an assessee is determined only at the end of the year, taxis required to be paid in advance in four instalments on the basis of estimated income i.e., on or before 15th June, 15th September, 15th December and 15th March.

However, residents opting for presumptive taxation scheme can pay advance tax in one instalment on or before 15th March instead of four instalments. In certain cases, tax is required to be deducted at source from the income by the payer at the rates prescribed in the Income-tax Act, 1961 or the Annual Finance Act. Such deduction should be made either at the time of accrual or at the time of payment, as prescribed by the Act.

For example, in the case of salary income, the obligation of the employer to deduct tax at source arises only at the time of payment of salary to the employees. However, in respect of other payments like, fees for professional services, fees for technical services, interest made to residents, the person responsible for paying is liable to deduct tax at source at the time of credit of such income to the accounts of the payee or at the time of payment, whichever is earlier. Such tax deducted at source has to be remitted to the credit of the Central Government through any branch of the RBI, SBI or any authorized bank.

Step 13: Tax Payable/Tax Refundable

After adjusting the advance tax and tax deducted at source, the assessee would arrive at the amount of net tax payable or refundable. Such amount should be rounded off to the nearest multiple of ` 10. The assessee has to pay the amount of tax payable (called self-assessment tax) on or before the due date of filing of the return. Similarly, if any refund is due, assessee will get the same after filing the return of income.

Income Tax as a source of revenue to the Government(State & Central):

There are two main sources of revenue to the Government namely,

1) Tax revenue

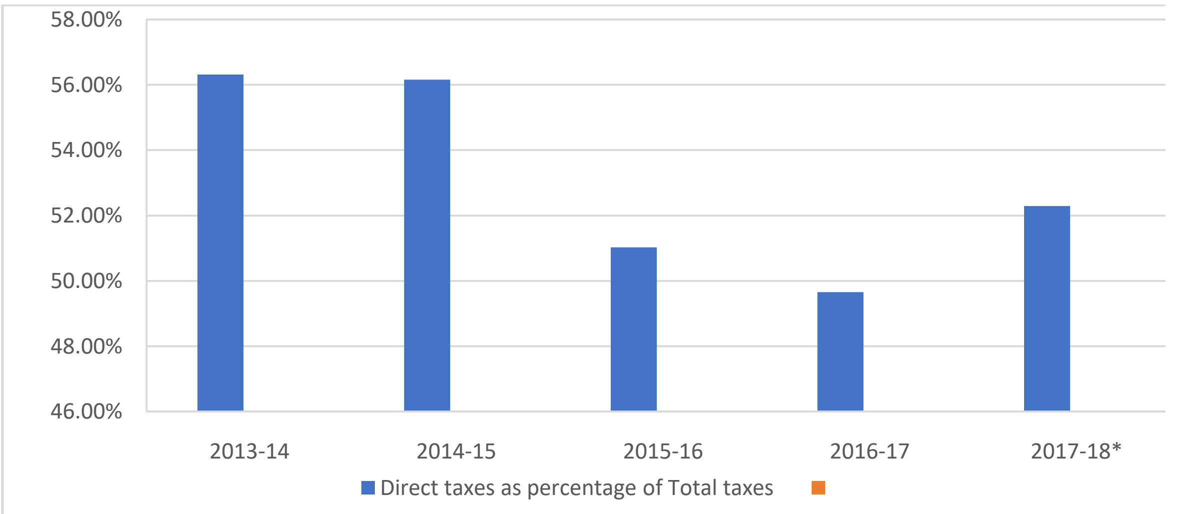
2) Non Tax revenue

Tax revenue : It consists of the proceeds of taxes and other duties levied by the government. As an important component of revenue receipts, tax revenue comprises direct taxes and indirect taxes. Direct taxes include taxes collected from individuals and corporate taxes.

Non Tax revenue : Revenue collected from sources other than tax sources is non tax revenue. It consists of interest receipts, profits from public sector undertakings, income from print and mint of currency, fees, fines, penalties and grants in aid from foreign countries and international organizations.

CONTRIBUTION OF DIRECT TAXES TO TOTAL TAX REVENUE (Rs. Crores)

Financial year	**Direct taxes**	**Indirect taxes**	**Total taxes**	**Direct taxes as percentage of Total taxes**
2013-14	638596	495347	1133943	56.32%
2014-15	695792	543215	1239007	56.16%
2015-16	741945	711885	1454180	51.03%
2016-17	849713	861515	1711228	49.65%
2017-18	1002741	915256	1918210	52.29%



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The direct taxes used to contribute 56.32% of Total tax revenue to the Government during the year 2013-14. Gradually percentage of the direct taxes to total tax revenue decreased. During these past 5 years for the financial year 2016-17 it was the least contribution by direct taxes to tax revenue for the government that is 49.65%. Again for the financial year 2017-18 it rose to 52.29%.

and spend that tax revenue on poor people in the form of subsidies, concessions, health, education etc. as public expenditure.

Recently the Advisor to the Governor KK Sharma said that " Taxation necessary for egalitarian, developed society." The Advisor said it is important that people pay their taxes on time as the same gets used for various developmental works which include constructions of schools, colleges, hospitals, bridges, macadamizing of roads and other like things. The Advisor said that the concept of taxation finds its root in our historical texts also and it has been used as a means for bringing a balance in the society so that equitable development of the society takes place and people enjoy the benefits of development. He said that the people by regularly filling their income tax returns are contributing their bit in building a strong and prosperous nation.

Impact of Income Tax on economic growth

The direct tax is one of the important sources of government revenue. Further it also impacts directly the disposable income of individuals. If direct tax rate is increased by the Government, people start saving for investment purposes. Due to this behaviour of individual's income generation process of economy is hampered. Particularly this is true for luxury commodities. This decreases the production of luxury commodities in the economy and as a result also adversely affects the GDP and standards of living.

One of the most commonly discussed issues in economics is how tax rates relate to economic growth. Advocates of tax cuts claim that a reduction in the tax rate will lead to increased economic growth and prosperity. Others claim that if we reduce taxes, almost all of the benefits will go to the rich, as those are the ones who pay the most taxes. What does economic theory suggest about the relationship between economic growth and taxation?

Income Taxes and Extreme Cases: In studying economic policies, it is always useful to study extreme cases. Extreme cases are situations such as "What if we had a 100% income tax rate?", or "What if we raised the minimum wage to Rs.5000an hour?". While wholly unrealistic, they do give very stark examples of what direction key economic variables will move when we change a government policy.

First, suppose that we lived in a society without taxation. We'll worry about how the government finances its programs later on, but for now, we'll assume that they have enough money to finance all the programs we have today. If there are no taxes, then the government does not earn any income from taxation and citizens do not spend any time worrying about how to evade taxes. If someone has a wage of Rs.100 an hour, then they get to keep that Rs.100. If such a society where possible, we can see that people would be quite productive as any income they earn, they keep.

Now consider the opposing case. Taxes are now set to be 100% of income. Any cent you earn goes to the government. It may seem that the government would earn a lot of money this way, but that's not likely to happen. If you don't get to keep anything out of what you earn, why would you go to work? Most people would rather spend their time doing something they enjoy. Simply, put, you wouldn't spend any time working for a company if you didn't get anything out of it. Society as a whole wouldn't be very productive if everybody spent a large portion of their time trying to evade taxes.

The government would earn very little income from taxation, as very few people would go to work if they did not earn an income from it.

While these are extreme cases, they do illustrate the effect of taxes and they are useful guides of what happens at other tax rates. A 99% tax rate is awfully like a 100% tax rate, and if you ignore collection costs, having a 2% tax rate is not much different from having no taxes at all. Go back to the person earning Rs.100 an hour. Do you think he'll spend more time at work or less if his take-home pay is Rs.80 rather than Rs.20? It's a pretty safe bet that at Rs.20 he's going to spend less time at work and much more time trying to earn a living away from the prying eyes of the government.

In the case where the government can finance spending outside of taxation, we see the following:

- Productivity declines as the tax rate increases, as people choose to work less. The higher the tax rate, the more time people spend evading taxes and the less time they spend on the more productive activity. So the lower the tax rate, the higher the value of all the goods and services produced.
- Government tax revenue does not necessarily increase as the tax rate increases. The government will earn more tax income at 1% rate than at 0%, but they will not earn

more at 100% than they will at 10%, due to the disincentives high tax rates cause. Thus there is a peak tax rate where government revenue is highest. The relationship between income tax rates and government revenue can be graphed on something called a *Laffer Curve*.

However on the positive sides, if proper deductions are allowed based on investments, it leads to capital formation in the country. Thus, broadly following are the positive impact on economic growth:

- Better capital formation
- Inducement of saving and investment
- Surety of Government's revenue growth
- Increase in planned expenditure of government
- Decrease in inflation rate due to lesser availability of disposable income to persons
- Timely availability of revenue to the Government

Major defects in the tax structure of India

High Rate and Low Yield of Direct Taxes: In India, as in other LDCs, the rate of direct tax is very high but the contribution to the total tax revenue is very low. In the 1950s, the rate of income tax in India was one of the highest in the world but the revenue was very insignificant. This is because high tax rates encouraged tax evasion and avoidance on a large scale. It may be noted in this context that tax avoidance refers to arranging one's financial affairs within the law so as to minimise taxation liabilities, as opposed to tax-evasion which is failing to meet actual tax liabilities through, e.g., not declaring income or profit. So the Government gradually reduced the tax rate over the years. In spite of this, the rate of income tax in India is one of the highest in the world even today. The higher tax rate (including surcharge and cess) at present is 42.7%.

Low Contribution of Income Tax: Although the rate of income tax is the highest in India, the contribution from such is very low. Tax evasion seems to be the primary reason. Another reason is the high exemption limit in a country where per capita income is very low. In India, the exemption limit has been raised from time to time, but the levels of national and per capita incomes have failed to increase proportionately. Consequently, more and more people have managed to come out of the tax net. India's per capita income in 2018-2019 was Rs. 126408(approx) at current prices but the exemption limit in case of personal income tax was Rs. 250000. If other deductions are brought into consideration (such as investment in approved Government securities such as NSCs , units of UTI , of public provident fund, or insurance policies), the exemption limit would be even more. It is a pity that the percentage of people paying income tax in India at present is less than one. Naturally, the major reliance is on indirect taxes. In fact, an undue reliance on indirect taxes is a common feature of the system of LDC's.

Absence of Agricultural Income Tax: Another feature of India's tax system is that there is no tax on agricultural income. Agriculture is the dominant sector of the Indian economy. The contribution of agriculture and related activities to India's GDP was 29.3% in 1999-00. Planned investment on agriculture has also increased over the years. But agriculture has failed to make any contribution to the introduction of the Government's tax revenue. Since agriculture is a State subject, the introduction of the agricultural income tax system at the Central level has not been possible. This is another reason for undue reliance on indirect taxes.

***Inequitable*:** The Burden of Indirect Taxes is more on poor people than Rich People. Moreover recent increase made in section 87A rebate that is Rs.12500 for the persons with income of Rs.500000 is inequitable as the person having income of Rs.500001 will end up paying tax as per earlier slabs where as person with income of Rs.500000 will not pay any tax. Further there is no distinction between person of age 80 years and person with age below 60 years.

Progressive Taxes on Income: The Government has made the system of direct tax progressive and progressiveness is considered desirable in the interest of equity and for reducing the disparities in the distribution of income and wealth. But progressive taxes encouraged tax evasion and avoidance and have failed to reduce inequalities of income and wealth.

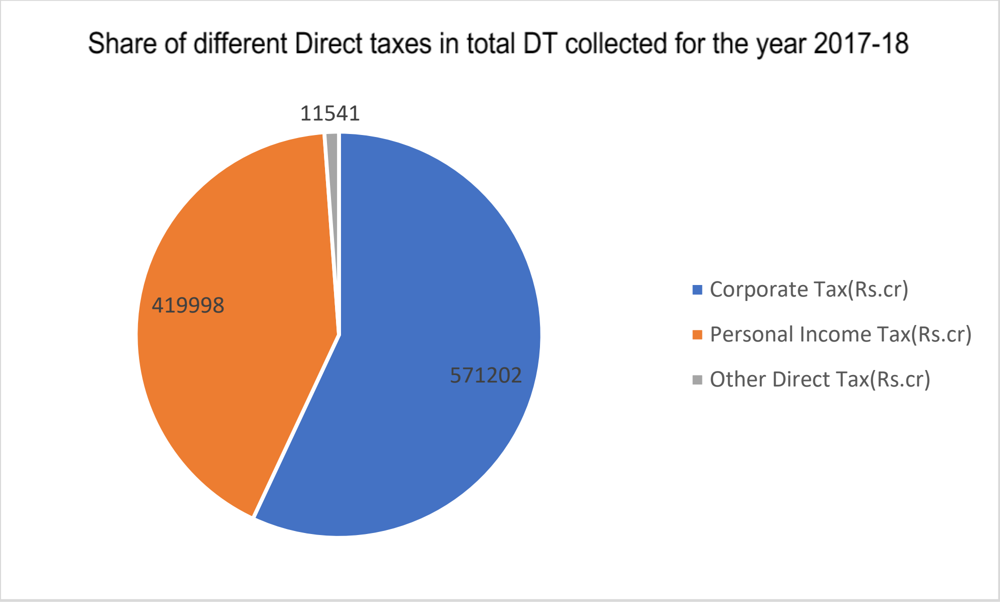
Data analysis

Tax collection *(Rs.Crores)*

Financial Year	Corporate Tax	Personal Income Tax	Other Direct Tax	Total
2013-14	394678	242888	1030	638596
2014-15	428925	265772	1095	695792
2015-16	453228	287637	1079	741945

2016-17	484924	349503	15286	849713
2017-18	571202	419998	11541	1002741

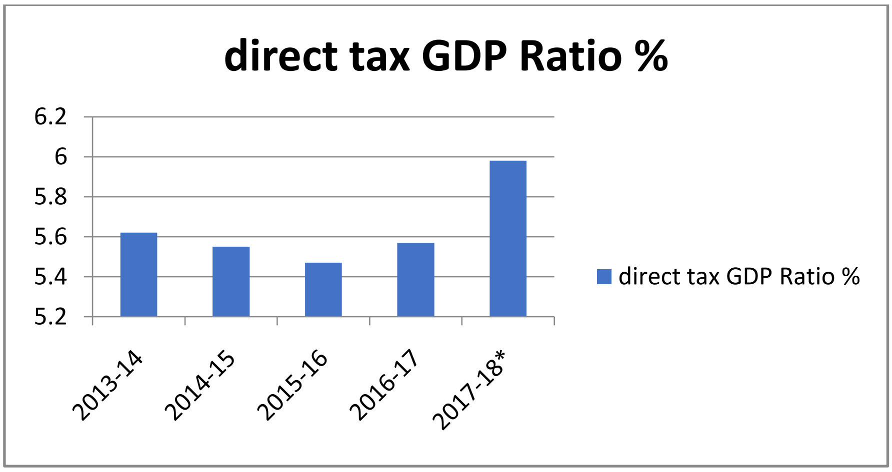
We can see that collection of direct tax increased in the past 5 years gradually. In the year 2013-14 it was Rs.638596 cores and rose to Rs.1002741 cores in the year 2017-18. Further corporate income taxes contribute a major part of the total direct taxes.



Above chart shows the contribution of corporate tax, personal income tax and other direct tax contribution to or share on total direct taxes. We can see that corporate taxes contribute a major part of the direct taxes collected by government during 2017-18.

Direct taxes and GDP ratio *(Rs. Crores)*

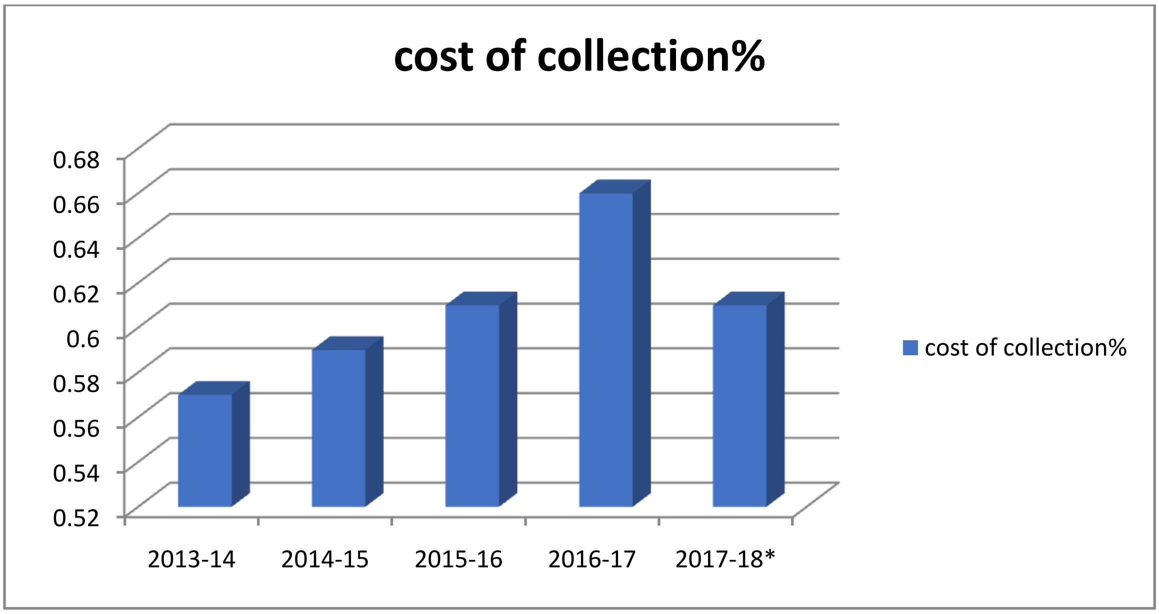
Financial year	Net Collection of Direct Taxes	GDP Current Market Price	Direct Tax GDP Ratio	GDP Growth Rate	Tax Growth Rate
2013-14	638596	11355073	5.62%	12.28%	14.24%
2014-15	695792	12541208	5.55%	10.45%	8.96%
2015-16	741945	13567192	5.47%	8.25%	6.63%
2016-17	849713	15253714	5.57%	12.43%	14.53%
2017-18*	1002741	16773145	5.98%	9.96%	18.03%



Direct tax GDP ratio refers contribution of direct taxes to GDP of country. We can see from above chart that Direct taxes GDP ratio was 5.62% in the year 2013 -14. It started decreasing gradually and in the year 2015-2016 it was least in the past 5 years I.e. 5.47%. Reason may be growth rate of direct taxes was less compared to growth rate of GDP growth rate as we can see in the above table. Then DT GDP ratio stared gradually increasing and it became 5.98% in the year 2017-18.

Cost of collection *(Rs. Crores)*

Financial Year	Total Collections	Total Expenditure	Cost of Collection
2013-14	638596	3641	0.57%
2014-15	695792	4101	0.59%
2015-16	741945	4593	0.61%
2016-17	849713	5578	0.66%
2017-18*	1002741	6087	0.61%



Cost of collection is the expense incurred to assess and collect tax.in the year 2013-2014 it was 0.57% and rose to 0.61% in 2017-2018 maybe due to inflation factor and new techniques adopted.

<u>Tax evasion v/s tax avoidance</u>

Every individual or assesse in a country dreams about to find a way in which he can avoid tax. He wants to use any means for the purpose of not paying or evading from tax. Tax Avoidance and Tax Evasion are two terms that serves a common purpose i.e. 'To reduce the amount of tax from person, firm or any legal entity's earnings" but one difference which can be drawn from these two concepts is that one aims to do it in a legitimate manner and other strives for an illegitimate manner. Tax Evasion and Tax Avoidance are two techniques which are used and applied by many people for the purpose of reducing their tax liability. These actions are performed only after consulting an expert in the field of tax. Tax avoidance is a completely legal procedure while Tax Evasion is considered to be crime in the whole world.

Tax Avoidance:

Any person who is able to avoid taxes is considered to be a wise guy. It is believed Tax Avoidance is a term which signifies a situation in which a taxpayer reduces his tax liabilities by taking advantage of the loopholes and ambiguities in the legal provisions. Since it is not illegal, tax avoidance is some sort of a legally allowable way to reduce the tax burden. It is not completely defined under Income Tax Act 1961.

Characteristics of Tax Avoidance:

Tax Avoidance is a way of reducing the taxes through the medium provided by government but before moving towards those ways, it is important to analyze tax avoidance from depth. Here are the following features for tax avoidance:

1. Tax Avoidance involves the legal exploitation of tax laws to one's own advantages.

2. Every attempt by legal means to prevent or reduce tax liability which would otherwise be incurred, by taking advantage of some provisions or lack of provisions in the statutes of the country.

3. An arrangement entered into solely by or primarily for the purpose of obtaining a tax advantages

Tax Evasion

Tax evasion is a crime in which an individual or a business entity intentionally underpays or hide their certain amount of income in order to save more amount of taxes. This method is certainly illegal in all the countries. Tax Evasion is basically non-payment of taxes by means of not reporting all taxable income, or by taking not allowed deductions. It originated in England between 1920 -1925

Activities relating to Tax Evasion

1. Under reporting income.
2. Inflating deductions or expenses.
3. Hiding Money.
4. Hiding interest in offshore accounts.

It is concluded from the above discussion that Tax Avoidance and Tax Evasion are those concepts which enables a person to avoid liability on his income tax charged. One concept is completely legal as provided under **Income Tax Act 1961** and another is a complete illegal. For the purpose of Tax Avoidance, Government has provided various ways in which a person can legally restrain tax on his income whereas on the other hand Government has given various penalties on the concept of Tax Evasion.

India has notified the inter-governmental agreement with the US for exchange of country-by-country (CbC) reports on multinational companies regarding income allocation and taxes paid in order to help check cross-border **tax evasion**.

Tax Evasion and Black money:

It is one of the main problems faced in India. People evade tax through illegal and unfair means. They may claim lesser profit, gains or turnover than the actual. They get the tax refunded, by making misrepresentation before the tax authorities.

Taxes being the major source of income for the Government, evading of tax causes economic inequality, many projects have be put on hold, welfare programs have to set aside. The reasons for the evasion of tax are that there is a high rate of taxation, failure to curb bribery, lack of simplified procedures (though the government is still in the process of simplifying the procedure), and lack of organized and systematic administrative structure.

One can evade income tax through non-reporting, underreporting and misreporting of income. The measures usually adopted to curb evasion of income-tax include non-reporting or underreporting of taxable income, maintaining multiple sets of books of accounts, knavish changes in books of accounts, keeping transactions out of books, opening and operating bank accounts under assumed frames, doing business in the names of dummies, over-reporting expenses, fragmenting income for reducing tax liability, under-invoicing sales and other transfer pricing manipulations.

Black Money: A country having flow of Black Money is also known as having a Parallel Economy through an illegal economic operation. The money, which is being made by the people without being accounted for it to the government, is known as Black Money.

Black Money has an impact on the economy as it provides us with the false information about the actual economy. Due to which the economic planning looses it's worth, because they are based on macroeconomic parameters, which completely ignore the black money. It will have a serious effect on the country's economic fiscal system as most of the Government income is based on the taxes collected.

As per the Direct Taxes Enquiry Committee "Black money and tax evasion, which go hand in hand, have the effect of seriously undermining the equity concept of taxation and warping its progressiveness. Together, they throw a greater burden to the economy."

The black money creates inequalities among people. The overall consumption pattern is titled in favour of rich and elite classes.

Consequences of tax evasion

- Tax evasion resulting in black money prevents the resource mobilization efforts of the Government. Shortage of funds distorts implementation of developmental plans and forces the Government to resort to deficit financing in case public expenditure is inelastic.
- Tax evasion interferes with the declared economic policies of the government by distorting saving/investment patterns and availability of resources for various sectors of the economy.
- Tax evasion undermines the equity attribute of the tax system. Honest taxpayers willingly bear disproportionate tax burden, feel demoralized and lured to join the tax evaders' camp.
- Tax evasion and black money encourage concentration of economic power in the hands of undeserving groups in the country which, in turn, is a threatening to the economy in its way.
- Evasion of tax consumes time and energy of tax administration to disentangle the intricate manipulations of tax dodgers.

- Unsocial activities like bribery, intimidation, blackmailing, tampering with official records, submitting fake documents, etc. are all abuses degrading social and moral values that ultimately go with tax evasion.
- Tax evasion has been causing reduction in country's economic growth
- The direct effect of tax evasion is the loss of revenue, and increase in inflation
- Black money has resulted in transfer of funds from India to foreign countries through clandestine channels which decrease country's reputation globally.
- Tax evasion leads to poor standards of living of the rural masses and the people BPL as the government cannot undertake welfare measures at the national level.
- It also brings disequilibrium in the economic condition of the country resulting in the rich becoming richer and the poor becoming poorer.
- Due to tax evasion of majority of the rich population, the government is forced to increase the rates of tax every assessment year for increasing its revenue which results in increased tax burden of those who pay taxes promptly

Comparison with other countries

Let's compare income tax paid in India with other countries. Indians earning more than Rs 10 lakh per annum pay over 30 per cent of their incomes as income tax, with an additional 4 per cent as cess. Those earning less than Rs 5 lakh a year pay no taxes while those in the income range of Rs 5-10 lakh pay 20 per cent tax, plus the 4 per cent cess.

China has four slabs of individual income tax-starting from 25 per cent for those earning between 9,000 to 30,000 yuan a month (Rs 90,000 to Rs 300,000 a month). It goes up to 45 per cent for monthly incomes of over 80,000 yuan. In the US, tax rates range between 22 per cent and 35 per cent. Several countries have higher personal income tax rates, such as Denmark, Sweden and Japan, but they provide an expansive social security net that includes state-run schools, healthcare, day care centres, unemployment allowance, housing et al.

TAXING TIMINGS

The government had to cut down expenditure for the shortfall in net tax revenue in final estimates compared to revised estimates presented in the budget presented on the 1st of February. Net tax revenue of Rs. 13.91 trillion was recorded in FY 2019 v/s the projected 14.84 trillion in the FY 20 budget. Direct tax revenue shortfall was Rs 747 billion and in Indirect taxes, the shortfall was sharper at Rs. 1.03 trillion or one lakh crore rupees.

Particulars	FY 2018 Actual	FY 2019 RE	FY 2019 Actual
Direct Tax	17.9 %	19.8%	12.3 %
Corporate Tax	17.8 %	17.5 %	16.2 %
Income Tax	18.1	22.8	7.2
Indirect Tax	5.8	14.3	3.1

At 35 per cent, corporate tax in India is among the highest in the world. In 1980, corporate tax rates around the world averaged 38.8 per cent, and 46.6 per cent when weighted by GDP. However, over time, countries realised the impact higher corporate tax rates have on business investment decisions. In 2018, the tax rates in most countries averaged between 23 and 26.4 per cent. The US, which until 2017 had the fourth highest corporate income tax rate in the world, introduced reforms in 2018 and lowered it towards the middle of the 208 countries surveyed for the International Tax Competitiveness Index. Most countries have corporate tax rates below 30 per cent even as India is holding on to the 35 per cent rate. Other countries levying such rates include Malta, the UAE and Puerto Rico.

In last year's budget, then finance minister Arun Jaitley had lowered corporate tax to 25 per cent for companies with a turnover of Rs 250 crore or less, partially fulfilling a promise made by the Narendra Modi government. Now, there is pressure on the government to reform India's corporate tax structure to remain globally competitive. Sliding investment by the private sector over the past few years presents a compelling case for a more globally-aligned tax policy for the corporate sector.

US President Donald Trump took a radical decision last year to lower corporate tax rates from 35 per cent to 21 per cent. If India continues with its high tax rate, it gives enough reason for major companies that create jobs and drive innovation to move towards lower tax jurisdictions. In April this year, during the Lok Sabha election campaign, Jaitley, though, had reiterated the promise of lowering tax rates.

Evidently there is a crisis of revenues that the government will have to deal with. In such a scenario, it should also refrain from excessive tax vigilantism. Start-ups have often complained about excessive tax policing. The government needs to realise that there is a fine line between effective tax administration and an intrusive administration. The Union budget will be a crucial test for the government as it battles a painful economic slowdown and a financial sector that is in disarray. The challenge will be of reviving growth and moderating government revenue.

Why only less than 2% of people pay tax in India.

We know that India is a country with 135.5 cr.(approx) but it is also true that hardly 2% of the individuals pay income tax in India. In the last four years, the government's efforts to widen the tax base resulted in an 80% jump in number of returns filed to 6.85 crore in 2017-18 from 3.31 crore in 2013-14. However, a large number of these individuals are paying no tax at all. As many as 2.02 crore individuals filed income-tax returns in 2017-18 declaring their income, but paid zero tax since they are not in the **taxable income bracket** yet, reported TOI. The number of such companies was 3.9 lakh.

The low numbers of people paying tax may indicate a large number of eligible people still evading taxes. At the last count, there were around 8.6 lakh doctors in the country, but less than half of them paid income tax. One in three chartered accountants — who advise individuals and companies on tax matters — paid income tax. While there are nursing homes every few km, only 13,000 paid taxes. In fact, their number is less than the number of fashion designers (14,500) paying income tax.

In fact, according to the data released by the I-T department on Monday, there is aa massive gap between the salaried, whose taxes are deducted, and the non-salaried. At Rs 5.2 lakh a year, the average annual income of the non-salaried is around 75% of salaried taxpayers, which adds up to Rs 6.8 lakh. The number of **salaried taxpayers** is rising at a faster pace than the non-salaried, although the count surprisingly is the same — 2.3 crore. On the positive side, over the last four years, there has been an increase of 27% in the income declared by the non-salaried, against a 19% increase in case of salaried.

The biggest contribution to the tax kitty comes from individuals who have paid tax up to Rs 5 lakh. As many as 2.55 crore filed returns in this bracket and paid Rs 1,21,384 lakh in tax. As many as 14,068 returns were filed in the above Rs 1 crore bracket which contributed Rs 35,464 crore. Only four people filed returns in the above Rs 100 crore bracket, paying Rs 665 crore in taxes.

2 CR INDIVIDUALS FILE RETURNS, BUT PAY ZERO TAX Another 2 cr pay tax but do not file returns

	INDIVIDUALS			COMPANIES		
Range of tax (₹)	No. of returns	Sum of tax payable (₹ cr)	Avg tax payable (₹)	No. of returns	Sum of tax payable (₹ cr)	Avg tax payable (₹)
Zero	2.02 cr	0	0	3.9 lakh	0	0
Up to ₹5 lakh	2.55 cr	1,21,384	47,602	2.9 lakh	2,825	97,749
Above 5L, up to 10L	5.57 lakh	38,314	6.9 lakh	34,842	2,485	7.1 lakh
Above 10 L, up to 25 L	2.6 lakh	39,004	15 lakh	34,264	5,449	15.9 lakh
Above 25 L, up to 1 cr	87,026	39,239	45.1 lakh	28,609	14,215	49.7
Above 1 cr, up to 50 cr	14,048	33,824	2.4 cr	18,782	1,02,529	5.5 cr
Above 50 cr, up to 100 cr	16	975	60.9 cr	412	28,669	69.6 cr
Above 100 cr	4	665	166.3 cr	466	2,39,549	514.1

Most returns and highest collection

Maharashtra and Delhi account for more than half of all income tax collections. However, their share is declining while those of Karnataka, Tamil Nadu and Gujarat — the other big contributors – is on the rise. However, at 38.3%, Maharashtra's contribution to the tax kitty is more than the next four states combined (Delhi 13.7%, Karnataka 10.1%, Tamil Nadu 6.7% and Gujarat 4.5%). Among the major states, Rajasthan has seen the fastest rise in tax collection, which have jumped more than three times in seven years.

On other hand in India agriculture income is wholly exempted from income tax under section 10. Poor tax collections, tax evasion, lack of information to the income tax department, bribery, corruption, many pending cases in court etc. are the other reasons for a low tax base in India.

Concepts of negative income tax

In economics, a **negative income tax** (**NIT**) is a welfare system within an income tax where people earning below a certain amount receive supplemental pay from the government instead of paying taxes to the government.

Such a system has discussed by economists but never fully implemented. According to surveys however, the consensus view among economists is that the "government should restructure the welfare system along the lines" of one. It was described by British politician Juliet Rhys-Williams in the 1940s and later by American free-market economist Milton Friedman.

Negative income taxes can implement a basic income or supplement a guaranteed minimum income system.

In a negative income tax system, people earning a certain income level would owe no taxes; those earning more than that would pay a proportion of their income above that level; and those below that level would receive a payment of a proportion of their shortfall, which is the amount their income falls below that level.

Flat tax with negative income tax

The effort for reporting and supervision can be significantly reduced by combining basic income with flat income tax. The relationship between gross and net income for individuals can be adjusted to correspond roughly to current relationship at all income levels, implying that income tax is effectively progressive.[9] A flat rate income taxation with tax exemption implements a negative income tax as well as maintaining an actual tax rate progression at extremely low administrative cost. This is achieved by paying a *tax on the tax exemption to all taxpayers*, e.g. in monthly payments. The tax on the tax exemption is computed by applying the nominal flat tax rate to the exemption. The tax on the income is drawn directly *from the source*, e.g. from an employer. The tax on income is computed by applying the nominal flat tax rate to the income.

This simple method results in an effective progressive rate taxation (although the tax rate for the taxes drawn at the source is flat) which is positive once the income exceeds the tax exemption. If, however, the income is less than the tax exemption, the effective progressive rate actually becomes negative without any involvement by any tax authority. As for the positive progression, only very high incomes would lead to an actual tax rate which is close to the nominal flat tax rate.

The tax on tax exemption also can be understood as a tax credit, which is paid back once an income has reached the level of the tax exemption. This level marks the point where paid taxes and the tax credit are equal. Above that point the state earns taxes from the taxpayer. Below that point the state pays taxes to the taxpayer.

Example:

- The income tax rate is 50%.
- The tax exemption is $30,000.
- The subsidy rate is 50% and equal to the income tax rate.

Under this scheme:

- A person earning \$0 would receive \$15,000 from the government.
- A person earning \$25,000 would receive \$2,500 from the government.
- A person earning \$30,000 would neither receive any money nor pay any tax.
- A person earning \$50,000 would pay a tax of \$10,000.
- A person earning \$100,000 would pay a tax of \$35,000.

Flat tax implementations *without* the provision of a negative income tax actually need an *additional* effort in order to *avoid* negative taxation. For such a tax, the exemption only can be paid after knowing the earned income. Flat tax implementations *with* negative income tax allow the payment or crediting of the income tax at any interval, independent of the amount of the actual income

Measures to improve tax collection

- Rewarding taxpayers and shaming non-payers
- Performance incentives for tax officials
- Integrating indirect tax database and portal with direct tax
- Adopting data mining technique to get relevant information to the income tax department
- Having a strong connection between income tax department and banks
- Encouraging cashless transactions which helps to reduce tax evasion
- Reducing the complexity of act and making user friendly portal for filling returns
- Trying to lower the rates to achieve high compliance

Conclusion:

Direct tax is an important source of income for the government as it contributes 52.29% to total tax revenue. India is a high rate and low compliance country. There are several defects present in the present tax structure of India. The recent hike in rebate under section 87A from financial year 2019-20 to Rs.12500(income upto Rs.500000) is having both pro's and con's. It will reduce the tax base in India. On other hand increase in surcharge on super rich may bring new revenue to the government. Even with the presence of many loopholes income tax is necessary to bring equality among people and for welfare of country. Government has to take proper actions to reduce the tax avoidance and evasion or else tax evasion may have a impact on economy.

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