

Inequality – Tax policy of India for Direct taxes and various facets of inequality

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Why inequality

- Legacy problems of inequality of opportunities:
 - ✓ disparity in access to resources
 - ✓ variations in access to education , health care etc
- Trickle down effect of growth in initial phases of economic development, not sufficient to arrest inequality (Kuznets curve-high inequality in countries in middle of development as indicated by per capita income ?)

Reducing inequalities –one goal and two simultaneous tax strategies

- Redistributive: get the rich to contribute more in taxes but calibrate tax rates to encourage work effort, promote investment -both domestic and foreign, support entrepreneurship and not induce tax evasion
- Growth stimulus : get the poor to earn more through tax preferences targeted to stimulate inclusive growth

Moving away from confiscatory rates

Year	PIT rate (MMR excluding surcharge and cess)
1957	91.8%
1958	84%
1971	97%
1978	84%
1984	67.5%
1985	50%
1997	30%
2011	30%

Supportive tax structure to reduce inequalities

- Redistributive policy
- ✓ high basic exemption limit in PIT
- ✓ a progressive rate schedule, reduced number of tax slabs (presently 3 - with fairly large range, to avoid bracket creep -against 11 in 1973-1974) in PIT
- ✓ flat rate for corporates (currently 30% i.e. equal to MMR for individuals +5% surcharge on tax for domestic companies with income exceeding Rs.10 million and 40%+2% surcharge for foreign companies) . Additional -3% education cess .Minimum Alternative Tax 18.5% +surcharge +education cess

Supportive tax structure to reduce inequalities

- Shift in share of Direct taxes in the tax revenue of Centre from 30.2% in 1995-1996 to 56.67% in 2010- 2011 manifests improved progressivity of tax structure
- Wealth tax on non productive assets and treatment of gifts of specified kind as income

Tax Revenue of Central Government

	1995-96	2002-03	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11(R)
Direct	33563 (30.2%)	83085 (38.4%)	157557 (43.0%)	219724 (46.4%)	295938 (49.9%)	319859 (52.8%)	377546 (60.5%)	446000 (56.7%)
PIT	17076 (15.4%)	36913 (17.1%)	56280 (15.4%)	75406 (15.9%)	103027 (17.4%)	106464 (17.6%)	132821 (21.3%)	149623 (19.0%)
CIT	16487 (14.8%)	46172 (21.3%)	101277 (27.7%)	144318 (30.5%)	192911 (32.5%)	213395 (35.3%)	244725 (39.2%)	296377 (37.7%)
Indirect	76806 (69.1%)	131284 (60.7%)	199348 (54.4%)	241538 (51.0%)	279031 (47.0%)	269433 (44.5%)	247357 (39.3%)	338978 (43.01%)
Customs	35757 (32.1%)	44852 (20.7%)	65067 (17.8%)	86327 (18.2%)	104119 (17.6%)	99879 (16.5%)	83324 (13.3%)	131800 (16.7%)
Excise	40187 (36.1%)	82310 (38.1%)	111226 (30.4%)	117613 (24.8%)	123611 (20.8%)	108613 (17.9%)	102991 (16.6%)	137778 (17.4%)
Service Tax	862 (0.8%)	4122 (1.9%)	23055 (6.3%)	37598 (7.9%)	51301 (8.6%)	60941 (10.1%)	58422 (9.4%)	69400 (8.8%)

1. PIT includes Taxes pertaining to expenditure, interest, wealth, gift, and estate duty.

2. The figures in bracket show respective percentage of Gross Tax Revenue.

Direct taxes and Indirect taxes as %of GDP

1	Financial Year	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
2	Corporate Tax	2.60	2.70	3.40	3.90	3.80	3.70	3.80
3	Personal Income Tax	1.60	1.50	1.70	2.10	1.90	1.90	1.90
4	Total Direct Taxes	4.20	4.30	5.10	6.00	5.70	5.60	5.70
5	Custom	1.80	1.80	2.00	2.10	1.80	1.30	1.50
6	Union Excise	3.10	3.00	2.70	2.50	1.90	1.60	1.70
7	Service Tax	0.50	0.60	0.90	1.00	1.10	0.90	0.90
8	Total Indirect taxes	5.40	5.40	5.60	5.60	4.80	3.80	4.00

Snap shot of Tax Returns for A.Y. 2010-11(F.Y. 09-10)

	Individuals (non-business)		Partnership & proprietorship		Companies	
Income Slab	% of returns filed	% of tax paid	% of returns filed	% of tax paid	% of returns filed	% of tax paid
0-10 lakh	51.04 (14433360)	4.58	43.98 (12435207)	5.35	1.42 (402858)	2.35
10-50 lakh	1.76 (498641)	6.42	0.77 (218564)	3.48	0.19 (53837)	1.27
50 lakh- 1cr	0.09 (24164)	1.38	0.08 (22658)	3.42	0.05 (15331)	0.99
1-10 cr	0.05 (12855)	2.13	0.06 (15698)	3.08	0.08 (21286)	5.51
> 10 cr	0.00 (315)	0.51	0.00 (1050)	2.34	0.02 (5665)	56.98

Direct Tax Collection

(in Rs. Crore)

Year	Collection	Growth %
• 2003-04	105088	
• 2004-05	132771	26.34%
• 2005-06	165216	24.44%
• 2006-07	230181	39.32%
• 2007-08	314330	36.56%
• 2008-09	333818	06.20%
• 2009-10	377546	13.10%
• 2010-11	446000	18.13%

Effective tax rate

Income for F.Y 2009-2010-

Statutory tax rate

Effective tax rate

CIT 33.99%

23.53%

PBT	Effective Tax Rate
Upto INR 1 crore	25.70%
Greater than INR 500 crore	22.55%

Efforts to actuate progressivity in taxes and meet distributional objectives

- Focus on formulating laws which are simple and easy to enforce and make compliance easy for taxpayers and counter tax avoidance surviving on exploitation of loopholes and ambiguities and treaty abuse
- Continuous review of tax preferences with a view to retaining only those that address market inefficiencies or generate positive externalities. Transparency in tax expenditure embedded in the tax statute ensured through yearly Revenue forgone Statement .
- Tax preferences to move from profit based to investment based as experience showed that the former were prone to abuse and had limited success in achieving targeted outcomes

Efforts to actuate progressivity in taxes and meet distributional objectives

- Wider tax withholding /third party information net to block nondisclosure/understatement of income. Tax identification number(PAN) made mandatory for large transactions and higher withholding tax provided for payees without PAN
- Technology enabled compliance by taxpayers accelerated ,through legislative interventions to reduce compliance cost and administrative burden and concurrently create a database to help policy formulation and target enforcement action based on information based risk profiling and risk assessment- E filing of tax returns, and e payment of taxes is mandatory for all corporates and large taxpayers and withholding tax statements by the deductors are also e filed
- Proper information systems built to enable 360 degree profiling of large income earners
- Processes modernised e.g. CPC and skill up gradation of employees ensured
- Dedicated institutional mechanisms set up to enforce compliance on shore and off shore

Efforts to actuate progressivity in taxes and meet distributional objectives

- LTUs –an initiative to provide better service and encourage compliance
- Cooperation across borders intensified to facilitate prompt and effective exchange of information including automatic exchange of information and assistance in collection of taxes; leadership role in global effort to counter tax evasion and harmful tax competition
- Build public opinion on tax compliance as an ethical norm – taxes build nation and tax evasion hinders development - tax evasion is linked to other harmful activities such as terrorism, drug trafficking, and corruption

Tax drivers to stimulate growth

- Some tax preferences for businesses in form of exemptions/deductions/accelerated depreciation to incentivise :
 - ✓ scientific research
 - ✓ exports
 - ✓ infrastructure development , power projects
 - ✓ location in specific areas
 - ✓ hospitals, housing projects , budget hotels
 - ✓ cold chain facilities ,processing/packaging/preservation/warehousing for agricultural produce
 - ✓ alternate energy

Some tax drivers to stimulate growth

- Tax preferences for individuals
 - ✓ long term savings and contribution to pension funds, payment of tuition fee for children , repayment of housing loan
 - ✓ health insurance premium
 - ✓ interest on loan for higher education
 - ✓ medical treatment of specified diseases/disabled dependents
 - ✓ rent for housing , interest for housing loan
 - ✓ lower tax burden on aged and women
 - ✓ Non-taxation of long term capital gains on stock exchange traded equity

Chasing a mirage- equality through taxes

- Taxes in isolation have a modest redistributive role
 - Taxes can in a limited way transfer resources to government for progressive spending or correct externalities
 - Progressivity in tax rate should not incentivize flight of capital and skilled labour
 - Excessive reliance on tax policy to stimulate growth can create vested interest groups and accentuate inequality

THANK YOU