ANNEX-7

Statement of Revenue Impact of Tax Incentives under the Central Tax System:
Financial Years 2022-23 and 2023-24

Tax law and its administration are primarily aimed at generating revenue to fund the various Government expenditures. The main variables that determine the amount of revenue generated are the collective tax base and the effective tax rates. An elaborate set of measures including special tax rates, exemptions, deductions, rebates, deferrals and credits determine these two variables. These measures are collectively called as 'tax incentives' or 'tax preferences'. They create an impact on Government earnings and also reflect the significant policy measures of the Government.

The tax incentives provided by the Government have a significant impact on its revenue. It may also be perceived as an indirect subsidy to the preferred taxpayers and is therefore referred to as 'tax expenditures'. In a democratic setup, tax policy is ought to be not only efficient but also sufficiently transparent. It requires an elaborate analysis and explicit presentation of tax incentives and the entailed program planning intended to address the specific policy goals of the Government. Further, transparent budgeting requires an analysis of revenue impact being created under the respective programme heads. These tax incentives having impact on the Government earnings are inherent part of the spending plans stated in the tax policy.

The present statement is a detailed analysis of the revenue implications of the various tax incentives provided by the Government through the taxation system. Such revenue implications of tax incentives were laid before the Parliament for the first time during Budget 2006-07 as Annex-12 of the Receipts Budget in the form of statement of Revenue Forgone. It was welcomed across all quarters and started the process of a constructive debate on whole range of issues concerning fiscal policy. It also lent credence to the Government's intention of bringing about transparency in the matter of tax policy and tax expenditures. The second edition of this statement was placed before Parliament during Budget 2007-08 by way of Annexure-12 of the Receipts Budget and also by way of a separate budget document titled "Statement of Revenue Forgone". Thereafter, it was placed every year before Parliament during Budget from 2008-09 to 2014-15. In the Budget 2015-16, it has been termed more appropriately as the "Statement of Revenue Impact of Tax Incentives under the Central Tax System", as it actually involves an analysis of the revenue impact. In Budget 2015-16 and 2016-17, it was made part of Receipt Budget as Annexure-15, while in Budget 2017-18, it was Annexure-13. In the Budgets 2018-19, 2019-20, 2020-21, 2021-22, 2022-23, 2023-24 and 2024-25, it was part of Receipt Budget as Annexure-7.

As stated earlier, this Statement seeks to list the revenue impact of tax incentives or tax subsidies that are a part of the tax system of the Central Government. The revenue impact of such tax incentives has been estimated in respect of most of the "tax preferences". The estimates are for financial year 2022-23, the most recent year for which data is available. It is based on the returns filed for the Assessment year 2023-24. An attempt has also been made to project the revenue impact for the financial year 2023-24 on the basis of the tax expenditure figures of the financial year 2022-23.

The estimates of the tax expenditures have been made on the basis of the following assumptions: -

(a) The estimates and projections are intended to indicate the potential revenue gain in case of removal of exemptions, deductions, weighted deductions and similar measures. The estimates are based on a short-term impact analysis. They are developed assuming that the underlying tax base would not be affected by removal of such measures. As the behavior of economic agents, overall economic activity or other Government policies could change along with the elimination of the specific tax preference, the revenue implications could be different to that extent.

(b) The impact of each tax incentive is determined separately, assuming that all other tax provisions remain unchanged. Many of the tax concessions do, however, interact with each other. Therefore, the interactive impact of tax incentives could turn out to be different from the tax expenditure calculated by adding up the estimates and projections for each provision.

Though the revenue impact has been quantified in terms of tax expenditure, it does not imply that this quantum of revenue has been waived by the Government. Rather, these could be seen as expenditure for the development of certain target sectors. In some cases, the socio-economic activities meant to be incentivized by such indirect subsidy may have either not been undertaken at all or have been undergoing at much lower scale in the absence of these incentives. The assumptions and methodology adopted to estimate the tax expenditure on account of different tax incentives are indicated at the relevant places in this Statement.

Direct Taxes

The direct tax policy through Income-tax Act, inter alia, provides for tax incentives to promote exports; balanced regional development; creation of infrastructure facilities; employment; rural development; scientific research and development; cooperative sector, encourage savings by individuals and donations for charity. Accelerated depreciation is also provided as an incentive for capital investment. Most of these tax benefits can be availed of by both corporate and non-corporate taxpayers. This statement attempts to estimate the revenue impact of the tax incentives separately in respect of all the categories of taxpayers viz., Corporate Sector; Non-Corporate Sector (Firms, Association of Persons, Body of Individuals etc.); and Individuals/ HUF. The heads under which the revenue impact has been estimated are broadly similar for the corporates and non-corporates. However, in the case of individuals, certain other heads have also been included as these are specific only to them. The statement for the corporate sector also analyses the spread of effective tax rates for companies in different profit slabs. A sectoral analysis of effective tax rates for different industries has also been attempted. Besides, details of entities engaged in charitable activities have also been provided separately under the head "Charitable Entities".

Revenue impact of various tax incentives for FY 2023-24 is projected by taking the average GDP growth for four years [FYs 2019-20, 2021-22, 2022-23 and 2023-24].[1]

A. Corporate Sector

Large businesses are mainly organized as companies. The Income-tax Department has received 10,75,866 corporate returns electronically up to 30th November 2024 for the financial year 2022-23 [i.e. assessment year 2023-24]. Every company is required to file its return of income electronically. These companies reported corporate tax liability of Rs. 7,27,415.89 crore [inclusive of surcharge and education cess] for their income of financial year 2022-23. The companies have paid additional tax of Rs. 6,440.99 crore [inclusive of surcharge and education cess] on their 'distributed income' on buy-back of shares under section 115QA of the Act.

For the purposes of estimating the tax expenditure, data pertaining to these companies were culled from the database for analysis and is detailed in Tables 1 to 5 and Appendix to this statement. **Table 1** profiles these companies across different profit ranges. The following facts emerge from an analysis of the data:-

- 5,34,092 companies (49.64 per cent) reported Rs. 32,10,198.19 crore as profits before taxes and a total income (taxable income) of Rs. 31,66,634.86 crore.
- 4,93,714 companies (45.89 per cent) reported Rs. 8,73,307.67 crore as losses.
- 48,060 companies (4.47 per cent) reported Nil profit.

The **effective tax rate[2] of the entire base of companies was 23.24 per cent** for financial year 2022-23 [as against

[1] *FY 2020-21 has not been taken for calculating the average GDP growth for it being an extraordinary year due to COVID-19 pandemic.*

[2] *Effective tax rate in case of companies is the ratio of total taxes [including surcharge and education cess to the total profits before taxes [PBT] and expressed as a percentage.*

the rate of **23.26** per cent reported in the financial year 2021-22] while the statutory tax rate was 31.20 per cent (inclusive of cess) in case of companies having income up to Rs. one crore, 33.38 per cent (inclusive of cess and surcharge) in the case of companies having income up to Rs. 10 crore and 34.94 per cent (inclusive of cess and surcharge) in the case of companies having income exceeding Rs.10 crore. Further, for existing companies which opted for the new concessional tax regime (lower tax rate without deductions and exemptions) under section 115BAA of the Income-tax Act, the statutory tax rate was 25.17 per cent. Companies with profits before taxes (PBT hereafter) of Rs. 500 crore and above, accounted for a total of 62.59 per cent of the total PBT and a total of 53.24 per cent of the total corporate income-tax liability.

The effective tax rate of companies with PBT greater than Rs. 500 crore is 19.77 per cent, which is lower than all the companies having profit before taxes below Rs. 500 crores. This highlights that the larger companies are availing the higher deductions and incentives or have shifted to the new regime of lower tax rate of 22 per cent plus cess and surcharge. This is further corroborated by the higher ratio of total income to PBT in smaller companies. In case of companies having PBT in range of rupees 0-1 crore, the ratio is 96.66per cent while in case of companies having PBT greater than rupees 500 crore, it is 72.45 per cent. A lower ratio indicates that the larger companies are availing higher deduction and incentives as compared to smaller companies.

Table 2 profiles the sample companies across effective tax rates. It is noted that 6,62,877 companies with average effective tax rates up to 20 per cent accounted for 39.68 per cent of total profits before taxes, 11.94 per cent of total taxable income and 13.52 per cent of total taxes. In other words, a large number of companies (6,62,877 i.e. 61.61 per cent) contributed a disproportionately lower amount of taxes in relation to their profits. Interestingly, 52,356 companies accounting for 6.58 per cent of the total profits and 10.40 per cent of the total taxes had an effective tax rate closer to the average statutory rate of 34.69 per cent. This shows that the tax liability across companies is unevenly distributed. This is primarily due to the various tax preferences provided in the statute that these companies avail.

It is further noteworthy that the 2,89,076 companies falling in bracket of effective tax rate of 20-30 per cent constitute more than 50 per cent (60.48 per cent) share in profit before taxes and contribute a significant portion of 71.71 per cent towards tax liabilities. The companies in this ETR bracket represent 26.87 per cent of total companies. This marks an increase of 4.5 per cent in the total tax share by these companies over that of 2021-22. The outcome is a significant indicator of the positive results of rationalization of corporate tax rates as introduced through the regimes contained in section 115BAA & 115BAB of the Income-tax Act, 1961.

*Effective tax rate (ETR) is inclusive of surcharge and education cess.

**The companies having ETR less than or equal to zero may report income under heads other than business, hence they have a small share of the total income and tax liability for corporates but may report ETR les than or equal to zero on account of brought forward losses.

Table 3 compares the effective tax rate of public companies (Public Sector Units only) with that of private companies. While the effective rate is lower than the statutory rate for both categories, the private sector companies pay a larger proportion of their profits as tax than the public sector companies.

Table 4 shows a comparison between the effective tax rate of the manufacturing sector and the other sectors in respect of the companies. The non-manufacturing sectors have a higher effective tax rate of 23.51 per cent as compared to manufacturing sector at 22.64 per cent. Both the sectors have an effective tax rate that is well below the average statutory rate of 34.69 per cent.

Table 5 gives details of the major tax expenditures on corporate taxpayers during the financial year 2022-23 and projection for the financial year 2023-24 The analysis is based on the corporate returns received up to 30th November, 2024, which includes all the returns filed for AY 2023-24. The revenue impact of each tax concession availed by these companies has been calculated by applying the weighted average statutory corporate tax rate of 34.69 per cent [3]on the amount of each deduction. The revenue impact of accelerated depreciation, deduction/ weighted deduction for expenditure on scientific research has been calculated by first determining the difference between the depreciation/ deduction debited to the profit and loss account by companies and the depreciation/ deduction allowable under the Income-tax Act. Thereafter the weighted average corporate tax rate of 34.69 per cent has been applied to this difference to arrive at the tax expenditure figure.

3 Average statutory tax rate has been worked out after taking a weighted average of the tax rate of 31.20 per cent in the case of companies having total income upto Rs. 1 crore, of 33.38 per cent in the case of companies having total income upto Rs. 10 crore and 34.94 per cent in the case of companies having total income exceeding Rs.10 crore.

Another aspect of tax expenditure is tax deferral. Tax deferral occurs when the taxpayer, on account of being allowed higher deductions under the tax statute is able to defer his tax liability by claiming an allowance (e.g. depreciation allowance) as a deduction over shorter time period whereas he may be spreading the same depreciation claim over a number of years in his own accounts. As depreciation does not entail cash outgo, this is a tax deferral. On the other hand, the MAT on companies under the tax statute fastens a liability (for the assessment year 2023-24, at the rate of 15 per cent on book profits), on the profit reported by the company to its shareholders (subject to some adjustments), if this liability is in excess of the tax liability computed at normal rates. The excess liability on account of MAT is allowed as a credit (up to 15 years) in a subsequent year in which the normal tax liability is in excess of MAT liability. The additional tax paid on account of MAT is, therefore, an advance payment of future tax liability. It restricts the period of deferral of taxes on account of claims of depreciation and moderates the revenue impact of other deductions such as profit-linked deductions by spreading the same claim over a longer period of time.

Based on the tax expenditure figures for the financial year 2022-23, the tax expenditure for the financial year 2023-24 has been projected by multiplying the tax expenditure on each tax incentive in the financial year 2022-23 by the average GDP growth for four years [FYs 2019-20, 2021-22, 2022-23 and 2023-24]. 2020-21 being Covid impacted year has not been considered. The average GDP growth rate was calculated to be 12.36 per cent.

Across various sectors, deductions availed by units located in SEZ (S. No. 1), accelerated depreciation (S. no. 2), Deduction of profits of undertakings engaged in generation, transmission and distribution of power (No.8), undertakings engaged in development of infrastructure facilities (S. No. 7), Deduction of profits of undertakings set-up in Sikkim (No. 18), Deduction in respect of employment of new workmen (No. 20), deductions on scientific research (S. No. 3), Deduction of profits of undertakings set-up in North Eastern State (No. 17), accounted for a significant portion of the total tax incentive. The deduction on account of donations to charitable trusts and institutions have marginally increased in F.Y. 2022-23 (Rs. 1172.93 crore) as compared to such donation in F.Y. 2021-22 (1132.90 crore).

The industry-wise distribution of effective tax rate of companies is given in the table in the Appendix to this statement. The effective tax rates for growing and manufacturing of tea (16.80), manufacturing of steel products (16.59), and manufacturing of refined petroleum products (18.30) are at the lower range. Some of the other sectors which are also having lower tax rates as compared to the effective tax rates are animal husbandry (15.61) and real estate (approx.18) The effective tax rate is the ratio of aggregate of gross tax payable to profit before tax.

Further in a effort to establish a globally competitive business environment for certain domestic companies, attract fresh investment, create employment opportunities and give an impetus to the overall economy, Section 115BAA and 115BAB had been inserted to the Act through Taxation Laws (Amendment) Act, 2019 (TLAA).It provides for a concessional tax rate of 22 per cent for existing domestic companies, and of 15 per cent for newly incorporated domestic companies which commence manufacturing or production on or before 31.03.2024 for manufacturing, production, research or distribution of such manufactured article or thing. This concession is subject to certain conditions including that they do not avail of any specified incentive or deductions. It has also been provided that the domestic companies opting for the concessional taxation regime shall not be required to pay any Minimum Alternate Tax (MAT).

An analysis of the impact of this concessional tax incentive (made in Table 5.1) shows that out of the corporate returns in the financial year 2022-23, the total income being taxed under section 115BAA of the Act is Rs. 18,35,988.38 Crore, which is an increase of 18.60 per cent over the income being taxed under the same section in the previous Financial Year 2021-22 (Rs. 15,48,040.43 Crore). Further, the total income taxed under section 115BAB of the Act is Rs. 6,256.74 Crore which is an increase of 165 per cent over the income being taxed under section 115BAB in Financial Year 2021-22 (Rs. 2,360.40 Crore). The number of companies adopting the new tax regime has also seen an increase Thus, the trend of adoption of the new concessional tax regime by companies has continued which is an encouraging sign.

B. Non-Corporate Sector [Firms/ AOPs/ BOIs etc.]

Apart from the corporate sector, large businesses are also organized as partnership firms and Association of Persons [AOPs] or Body of Individuals [BOIs]. The tax expenditure on these is not as large as that of companies. The Income-tax Department has received 18,21,249 returns filed electronically up to 30th November, 2024 for income of the financial year 2022-23. For the purposes of calculating the tax expenditure, data pertaining to these 18,21,249 Firms/ AOPs/ BOIs was culled out from the database.

The data was analyzed and the following facts emerged: -

- The entire firms/ AOPs/ BOIs declared a total income (taxable income) of Rs. 5,18,972.72 Crore and reported Rs. 3,92,120.64 Crore as profits before taxes and. Losses were reported in about 3,60,745 returns which is 19.81 per cent of the total.
- These firms/ AOPs/ BOIs reported Rs 1,30,916.68 Crore as income-tax payable [inclusive of surcharge and cess] for the Financial Year 2022-23.

The revenue impact of each tax concession claimed by the firms/ AOPs/ BOIs has been calculated by applying the income tax rate of 34.09 per cent (weighted average rate calculated taking rate of 31.20 per cent for firms having income less than one crore and 34.94 per cent for firms having income more than one crore with the gross tax payable falling in each tax rate slab) on the amount of each deduction. The tax expenditure on account of accelerated depreciation; deduction/ weighted deduction for expenditure on scientific research has been calculated by first determining the difference between the depreciation/ deduction debited to the profit and loss accounts by firms/ AOPs/ BOIs and the depreciation/ deduction allowable under the Income-tax Act. Thereafter, the income tax rate of 34.09 per cent has been applied to this difference to arrive at the revenue impact of each tax incentive. Based on the revenue impact for each tax incentive for the financial year 2022-23, the revenue impact for the financial year 2023-24 has been projected. The estimation for 2023-24 has been made by multiplying the tax expenditure on each tax incentive in the financial year 2022-23 by the average GDP growth for four years [FYs 2019-20, 2021-22, 2022-23 and 2023-24]. The average GDP growth rate was calculated to be 12.36 per cent. *

Table 6 depicts the major tax expenditures on non-corporate taxpayers in terms of tax expenditure during the financial year 2022-23 and projection for the financial year 2023-24. Like Financial Year 2021-22, the highest tax expenditure continues to be on account of deduction of profits of cooperative societies which accounts for 53.25 per cent of the total revenue impact as compared to 53.89 per cent in last financial year. The tax expenditure on account of units setup in SEZs (under section 10AA), housing projects (under section 80-IBA) and accelerated depreciation (under section 32) were 17.48 per cent, 11.46 per cent and 5.71 per cent of the total revenue forgone, respectively.

The total tax expenditure for non-corporate sector, i.e., Firms/ AOPs/ BOIs for the financial year 2022-23 is worked out to be **Rs. 10,920.83 Crore.**

C. Individual/ HUF Taxpayers

Chapter VI-A of the Income-tax Act primarily provides for deduction on certain payments and deduction on certain incomes. Individual/ HUF taxpayers are eligible to claim these deductions and have a wide range of tax preferences available to them. However, since more than 50 per cent of the individual taxpayers derive their income primarily from salaries, the profit-linked deductions [i.e. deduction on certain business incomes] are not claimed by them. On the other hand, the group of non-salaried individuals claims both type of deductions. The tax incentives granted to individual taxpayers is presented in Table 7. The tax impact under various sections of Chapter VI-A of the Income-tax Act has been calculated on the basis of various claims for tax preferences in the 7,74,07,645 returns filed electronically by individuals with the Income-tax Department till 30th November, 2024.

Based on the tax expenditure figures for financial year 2022-23, the tax expenditure for the financial year 2023-24 has been projected by multiplying the tax expenditure on each tax incentive in the financial year 2022-23 by the average GDP growth for four years [FYs 2019-20, 2021-22, 2022-23 and 2023-24]. The average GDP growth rate was calculated to be 12.36 per cent.

Based on the figures of total **7,74,07,645** returns of income filed for F.Y. 2022-23 (AY 2023-24), the tax expenditure for the entire population of taxpayers has been prepared. Some of the significant findings are as under: -

(i) Impact of higher basic exemption limits, (Sl. No. 27 and 28 of Table 7), has been calculated by multiplying the tax expenditure per senior citizen and very senior citizen with their respective numbers. According to the data of these returns, 12.05 per cent of the returns were filed by senior citizens and 0.79 per cent of the returns were filed by very senior citizens. Further, the revenue impact of higher exemption limit available to senior citizens has been calculated by taking into account the difference between the higher basic exemption limit (i.e. Rs. 3,00,000) as compared to the general exemption limit of Rs. 2,50,000 and applying the lowest tax rate of 5 per cent (plus cess) on the difference.

(ii) In case of individuals, the maximum tax expenditure of an amount of Rs. 1,02,557.01 Crore is on account of claim of deduction for investments in certain instruments as per section 80C of the Act.

(iii) The other major tax expenditure on individual taxpayers in the Financial Year 2021-22 is on account of rebate under section 87A amounting to Rs. 41,237.43 Crore.

(iv) Deduction on account of contribution to the New Pension Scheme under section 80CCD, and deduction on account of health insurance premium under section 80D also had a contribution of Rs. 14,999.41 Crore and Rs. 12,719.50 Crore respectively to the overall figure.

As detailed above, Table **7** depicts the revenue impact of major tax incentives for individual/ HUF taxpayers, in terms of tax expenditure, during the financial year 2022-23 and projection for financial year 2023-24.

The revenue impact of providing a tax incentive for investments in various savings instruments, repayment of housing loan and payment of tuition fees for children [all these come under section 80C of the Income-tax Act] is the single largest tax expenditure in case of individual taxpayers followed by rebate on tax in case of resident individuals having income up to five lakh rupees, contribution to New Pension Scheme (Section 80CCD) and deduction on account of health insurance premium (section 80D). The tax expenditure on account of higher basic exemption limits for senior citizens and very senior citizens are also significant. As regards profit-linked deductions, the highest tax expenditure is on account of section 80-IA and section 80-IBA of the Income-tax Act.

D. Charitable Entities

The Income-tax Act provides for exemptions to various entities including Government funded entities engaged in objects which are charitable in nature. In addition to this, specific exemption is also available to entities engaged in certain activities which satisfy social purposes. These entities receive donations, voluntary contributions and have other incomes from activities which are charitable in nature. The total receipts of such entities are required to be applied for the purposes for which these have been set up. These entities are required to file income tax return. The total number of electronically filed returns of such entities till 30th November 2024 for the assessment year 2023-24 is 2,50,682. The total amount applied by such entities for charitable and religious purposes during the FY 2022-23 is Rs 10,01,572.04 crores.