**2. Taxation**

**Highlights**

* Personal Income Tax rate for individual assesses with annual taxable income of Rs. 2.5 lakh to Rs. 5 lakh reduced from 10 % to 5 %.
* A surcharge of 10 % of tax payable on categories of individuals whose annual taxable income is between Rs. 50 lakh and Rs. 1 crore; the existing surcharge of 15 % of tax payable on people whose annual earning is more than Rs. 1 crore would continue.
* Corporate Income Tax rate has been reduced from 30 % to 25 % for Micro, Small and Medium Enterprises (MSMEs) with annual turnover of up to Rs. 50 crore.
* Time period for Long Term Capital Gains tax for property reduced to two years from earlier three years; the base year for indexation is proposed to be shifted from 1.4.1981 to 1.4.2001 for all classes of assets including immovable property.
* A simple one-page form to be filed as Income Tax Return for the category of individuals having taxable income up to Rs. 5 lakh other than business income.
* Basic customs duty on LNG reduced from 5 % to 2.5 %.

**Introduction**

Following the demonetisation drive of the government and the ensuing hardships faced by a wide section of the population, many had expected that the Union Budget 2017-18 will bring forth major changes in tax rates, threshold limit of taxation, tax exemptions, etc. Indeed the Budget does contain some changes on the tax front, mainly in the arena of direct taxes. The most important of these is the tax relief provided in the form of reduction in personal income tax rate levied on the lower-middle income tax payees. At the other end of personal income tax rate, a welcome move has been the levying of a surcharge of 10 percent on those whose annual taxable income is between Rs. 50 lakh and Rs. 1 crore. Another move in the right direction relates to the reduction in corporate income tax rates for MSMEs with annual turnover up to Rs. 50 crore.

**Revenue Projections and Tax - GDP Ratio**

The reduction in some of the tax rates notwithstanding, there has been a significant increase in revenue projections of the government, with tax revenues (i.e. gross central taxes) increasing by more than Rs. 2,00,000 crore in 2017-18 (BE) when compared to 2016-17 (RE). Further, nearly 64 percent of the projected growth in tax revenues is on account of direct taxes, with personal income tax accounting for the bulk of the growth in direct taxes (Table 2.1).

**Table 2.1: Growth in Tax Receipts in 2017-18 (BE) over 2016-17 (RE) (%)**

|  |  |
| --- | --- |
| Tax Components | Growth |
| Gross Tax Revenue | 12.2 |
| Corporation Tax | 9.1 |
| Taxes on Income | 24.9 |
| Wealth Tax | 34.0 |
| Customs | 12.9 |
| Union Excise Duties | 5.0 |
| Service Tax | 11.1 |
| Taxes on Union Territories | 9.4 |

*Source:* Union Budget 2017-18.

As a result, as Table 2.2 shows, not only is the Gross Central Tax to GDP ratio estimated to cross the 11 percent mark, the projected direct tax to GDP ratio (within central taxes) is also one of the highest in many years. However, the picture of progressivity in taxes can be misleading when we consider only Central Government tax receipts. In this context, it should be noted that when the overall tax collections of both the Centre and the States are taken into account, nearly two-third of total tax collected is accounted for by indirect taxes, implying that the tax structure in the country continues to be regressive.

**Table 2.2: Gross Central Tax - GDP Ratio (%)**

|  |  |  |  |
| --- | --- | --- | --- |
| Year | Gross Tax-GDP Ratio | Direct Tax-GDP Ratio | Indirect Tax-GDP Ratio |
| 2012-13 | 10.4 | 5.6 | 4.8 |
| 2013-14 | 10.1 | 5.7 | 4.4 |
| 2014-15 | 10.0 | 5.6 | 4.4 |
| 2015-16 | 10.6 | 5.4 | 5.2 |
| 2016-17 (BE) | 10.8 | 5.6 | 5.2 |
| 2016-17 (RE) | 11.3 | 5.6 | 5.7 |
| 2017-18 (BE) | 11.3 | 5.8 | 5.5 |

*Notes:*

1. Direct taxes such as estate duty, gift tax have not been taken into account as they form negligible proportion of direct taxes.
2. Taxes on Union Territories also have been taken into account in the calculation.

*Source:* Compiled by CBGA from Union Budget documents, various years.

**How optimistic are the Projected Revenue Figures?**

There are several reasons to question the huge increases in the revenue projections for 2017-18. For one, as past experience shows, there is usually a shortfall in actual tax collections compared to the budget estimates or even the revised estimates. This was true even for the year 2015-16 in the case of direct taxes. Therefore, even the projections for 2017-18 (BE), especially in the case of direct taxes, might be on the higher side. Second, the likelihood of the projected numbers being on the higher side is further compounded by the fact that this is the first year that the revenue data provided by the government is based only on the first nine months of the year. Third, a part of the quantum jump in the rate of growth of direct tax collections at around 35 percent can perhaps be explained by the use of demonetised notes to pay advance taxes. If this is indeed so, then it cannot be taken as a basis for projecting tax collections for the entire year. Even the projections for indirect tax collections could be questioned. This is because while in the previous year a large part of excise duty collections were due to windfall provided by higher global oil prices, the slowing down of the economy in the post-demonetisation period is likely to dampen tax collections from this source.

While the discussion above refers to projected tax revenue, even the projections for miscellaneous capital receipts, comprising disinvestment receipts, strategic disinvestment and others (listing of insurance companies), could be on the higher side given that only a small part of the strategic disinvestment projected in 2016-17 (BE) actually fructified in 2016-17 (RE). Further, given the problem of slowing investment demand facing the economy (large unutilised capacity across a number of sectors being a reflection of this problem), the actual disinvestment receipts might be very different from the figures projected in 2017-18 (BE).

**Table 2.3: Union Government’s Miscellaneous Capital Receipts (Rs. Crore)**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | 2015-16 | 2016-17 (BE) | 2016-17 (RE) | 2017-18 (BE) |
| Disinvestment Receipts | 42131.69 | 36,000 | 40,000 | 46,500 |
| Strategic Disinvestment | ... | 20,500 | 5,500 | 15,000 |
| Others (Listing of Insurance Companies) | ... | ... | ... | 11,000 |
| Total | 42131.69 | 56500 | 45500 | 72500 |

*Source:* Compiled by CBGA from Union Budget documents, various years.

**Tax Administration**

It may well be argued that a part of the increase in revenue projected in 2016-17 (RE) and 2017-18 (BE) can be explained by the improved tax compliance following demonetisation; however, it also needs to be kept in mind that human resource for tax administration plays an important role in improving tax compliance. However, the shortage of human resources[[1]](#footnote-1) in the Income Tax Department, with the overall vacancy being as high as 30 percent of the sanctioned strength[[2]](#footnote-2), may further derail tax collections. In short, the voluminous growth expected in overall receipts and direct tax collections seems like a tall claim.

**Revenue Foregone Due to Exemptions in the Central Tax System**

**Table 2.4: Some Important Declarations in Union Budget 2017-18**

|  |  |
| --- | --- |
| *Tax incentives* | *Revenue Foregone (Rs. Crore)* |
| Tax rates for MSMEs with turnover up to Rs. 50 crore reduced | 7,200 |
| Personal income tax rate cut for those falling in the tax slab between 2.5 lakh to 5 lakh | 15,500 |
| Total net revenue foregone because of exemptions in direct taxes | 20,000\* |

*Note*: \*The government expects to raise Rs. 2,700 crore from the 10% surcharge to be levied on annual taxable income between Rs.50 lakh to Rs. 1crore and the already existing 15% surcharge on income above Rs 1 crore.

*Source:* Budget Speech, Union Budget 2017-18.

The total revenue foregone, due to the exemptions / concessions/ deductions in the central government tax system, is projected to be Rs. 3.18 lakh crore in the year 2016-17, which is 2.1 percent of the country’s GDP. The trend in (estimated) revenue foregone as a percent of GDP is presented in the figure below.

**Figure 2.1: (Estimated) Revenue Foregone in the Central Tax System as % of GDP (2011-12 to 2014-15)**

*Source:* Compiled by CBGA from Union Budget documents, various years.

**Figure 2.2: (Estimated) Revenue Foregone in the Central Tax System as % of GDP (2015-16 to 2016-17)**

*Source:* Compiled by CBGA from Union Budget documents, various years.

As is clear from Figure 2.1 and Figure 2.2, there has been a sharp drop in the revenue foregone to GDP ratio from 4.5 percent in 2014-15 to 2.1 percent in 2016-17. This decline is primarily owing to lower estimates of revenue foregone on account of excise duty and customs. Between 2014-15 and 2015-16, the estimated amount of tax foregone on account of excise duty fell from Rs. 2 lakh crore to Rs. 70,000 crore, and, in the case of customs, tax foregone fell from Rs. 2.4 lakh crore to Rs. 80,000 crore.

However, as mentioned in the Union Budget 2017-18, this decline is mainly due to a change in the methodology for estimating revenue foregone in excise and customs. Therefore, the revenue foregone estimates for the years up to 2014-15 are not strictly comparable with the estimates for the subsequent years.

As mentioned earlier, the total revenue foregone projected for 2016-17 amounts to 2.1 percent of GDP. When compared to the projected fiscal deficit of 3.2 percent of GDP in 2017-18 (BE), the revenue foregone amount does seem like a largesse that may not always be justified. The purpose of providing tax incentives can sometimes be self-defeating, as all tax incentives do not necessarily lead to development. If some of the tax incentives provided (particularly to the corporate sector) could be rationalised, it may have significant impact on the total revenue earnings of the government and create additional fiscal space permitting enhanced public expenditure.

1. This is true for officials at various levels such as additional tax commissioner, deputy tax commissioner and income tax officials. [↑](#footnote-ref-1)
2. # Cited in Sruthisagar, [Yamunan](https://scroll.in/authors/11457), 2017, ‘Demonetisation adds to Income Tax Department's Workload, even as it struggles with a Staff Crunch’, January 3, 2017, available at: https://scroll.in/article/821881/demonetisation-adds-to-income-tax-departments-workload-even-as-it-struggles-with-a-staff-crunch

   [↑](#footnote-ref-2)