A NOTE ON KEY ISSUES RELATED TO THE INDIAN TAXATION REGIME
Centre for Budget and Governance Accountability (CBGA) and Confederation of Voluntary Associations (COVA) 2012

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1. Stepping up the Tax-GDP Ratio for the country

The total tax revenue collected by Centre and States (combined) has fallen from (the already low level of) 17.4 % of GDP in 2007-08 to 14.7 % of GDP in 2010-11 (BE)[1]. India's tax-GDP ratio compares poorly against those of several other countries such as Sweden 50.1%, Brazil 34.2% Russia 32.3% and UK 27.3%,. Hence, it is necessary to take strong measures for stepping up the country's tax-GDP ratio, which would enable provision of more resources for budgetary spending on social sector that alone could ensure crucial entitlements and access to basic services to the people.

Policy Required: Bringing tax- GDP ratio to at least 20% in the next 5 years and 30% by 2025

2. Moving towards a progressive taxation regime: Need to rely more on Direct Taxes instead of Indirect Taxes

Of the total tax revenue of our country, while indirect taxes (that affects the poor more) account for 9.25 % of GDP, direct taxes account for only 5.48 % of GDP[2]. If India is to move towards a more progressive tax system, the government should rely more on direct taxes (such as, corporation tax, personal income tax and wealth tax). The proposed Direct Tax Code (DTC) does nothing to move towards a more progressive tax regime and further exacerbates the regressive nature of taxation in the country. Some key objectionable points from DTC that could contribute to making the system more regressive to be mentioned here.

Policy Required: New ratios to be proposed- examples from some other countries with acceptable DTC to be given.

3. Probing the Justification for Tax Exemptions and Reducing the Magnitude of Revenue Foregone

The total magnitude of tax revenue forgone due to exemptions/ deductions/ incentives in the Central Government tax system is estimated (by the Union Ministry of Finance) to be Rs. 5,29,432 crore in 2011-12. Tax exemptions need to be minimised, carefully designed and justified with sound social and economic reasons. Even if half of the tax revenue forgone presently because of the plethora of exemptions in the Central Government tax system get collected, it would generate additional tax revenue worth 3 % of GDP- enough to provide balance resources required for successful implementation of the entire RTE program . If the entire tax revenue being forgone amounting to 6% of the GDP is collected, then this could provide universal education and health facilities for all Indian citizens.

Policy Required: Announcement of a more rigorous and transparent Tax exemption policy.

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[1] Indian Public Finance Statistics, 2010-11, Govt. of India

[2] Indian Public Finance Statistics, 2010-11, Govt. of India

4. International Taxation Loopholes to address Tax Evasion and Tax Avoidance

a) Plugging the Loophole in India-Mauritius Treaty: According to the tax treaty between India and Mauritius, a company resident in Mauritius selling shares of an Indian company will not pay tax in India. Since there is no capital gains tax in Mauritius, the gain will escape tax altogether[3]. With approximately 40% of FDI equity inflows coming from Mauritius, it is important that this loophole is fixed definitively.

b) General Anti-Avoidance Rules (GAAR): Effective GAAR will ensure that the real intention of the parties and effect of transactions and purpose of an arrangement is taken into account for determining the tax consequences, irrespective of the legal structure that has been superimposed to camouflage the real intent and purpose. It is also important to take a stand on the issue of GAAR (General Anti-Avoidance Rules) overriding treaties until the India-Mauritius treaty can be amended to close the tax loophole definitively.

Extent of revenue loss to the exchequer in the last 3 to 5 years due to (a) and (b) to be cited if possible- what it could mean in terms of providing services to the poor could be stated

Policy required:

What could your Party gain by announcing a Progressive Tax Regime:

If your party announces the formulation of a progressive tax regime by bringing appropriate changes in improving Tax GDP ratio, increased reliance on Direct Taxes and reduction of Indirect Taxes, reducing tax exemptions to corporates and the rich and by plugging loopholes in international taxation policies to address tax avoidance and evasion, then the combined revenues that could be generated could be to the tune of _____

With this additional resource base, your party could announce and ensure the following facilities and programs for the poor;

1. Universal education
2. Universal health care
3. Right to food for all Indians below poverty line
4. Free water supply
5. Sanitation
6. Improved standard of living for the poor with reduced taxes and increase in services that could lead to bringing the HDI to below 100 from the present 134 in 2011.

3 http://www.frontlineonnet.com/stories/20120323290501700.htm