



## PERSPECTIVES ON TAX DESIGN AND TAX REFORM

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### Abstract

*Tax design is a complex and ongoing process aimed at balancing the need for revenue to fund public goods and services while minimizing the economic burden on taxpayers. It involves considering the potential impact of taxes on the economy, such as their effect on economic growth, investment, and job creation. In India, tax design has been a critical aspect of public finance and economic policy since its independence in 1947, with the most recent reform being the introduction of the Goods and Services Tax (GST) in 2017. This paper examines the tax design and structure of India, focusing on the various reforms that the country has undergone. Specifically, it critically analyses the impact of these reforms, particularly the introduction of GST, on the Indian economy. The findings highlight the positive effects of these reforms, such as improving the ease of doing business and increasing tax revenue. However, the paper emphasizes the need for ongoing efforts to ensure transparency, fairness, and equity in the tax system for all taxpayers. Through this analysis, the paper provides insights into the role of tax design and reforms in driving economic development in India.*

**Keywords** – GST, VAT, GDP Ratio, tax Evasion, tax reforms.

### I. ARTICLE REVIEW

The article "Tax Policy and Reforms in India"<sup>1</sup> examines the country's present tax structure and highlights the country's ongoing tax reform efforts. To build a straightforward, predictable, and transparent tax system, it emphasizes the principles of optimum tax theory that advocates on expanding the tax base, lowering tax rates, and minimizing rate discrepancies. These changes are meant to boost income while lowering collection expenses and distortions.

It further compares these concepts to the current situation of the Indian tax system, which it claims is underperforming due to a low tax-GDP ratio. The tax exemption for agricultural income, which reduces the tax base and

creates opportunities for evasion, is one of the causes. The government's refusal to collect the tax on agricultural incomes and the assignment of that tax to them has resulted in major tax evasion and avoidance, frequently through misclassification.

The author here also contends that the development of tax preferences in direct and indirect taxes to accomplish numerous goals diminishes compliance, narrows the base, and confuses the system. Another significant source of lost revenue is the wilful evasion of multinational corporations with headquarters in tax havens. The article also emphasizes the necessity for the tax administration to have more capacity to handle intricate company systems.

<sup>1</sup> Rao, M. Govinda, 'Tax Policy and Reforms in India', *Studies in Indian Public Finance* (Oxford, 2022; online edn, Oxford Academic, 19 May 2022), <https://doi.org/10.1093/oso/9780192849601.003.0004>

Montek Ahluwalia, in an article on Economics reforms,<sup>2</sup> outlines the economic reforms carried out by the present government in India under Prime Minister Narendra. The article focuses on the social concerns that the government and opposition parties disagree on, particularly the rise in violence against Dalits and minorities. It is further discussed in this article that the Modi administration's commitment to maintaining a liberal industrial policy, openness to foreign trade and FDI, infrastructure improvement, and digital IT infrastructure development are among the key efforts covered in the article. The government's Goods and Services Tax (GST) system, which has drawn criticism for being overly complicated and having too many rates, is the biggest reform to date. These issues have been recognized by the government, and solutions are anticipated in the future.

The article also highlights the introduction of the "Insolvency and Bankruptcy Code", which attempted to make the debt recovery process faster from the companies that defaulted in repayment.

### Analysis

#### II. Tax Design in India

The Indian tax system is characterized by its dual nature of being progressive and proportional. The slab-wise taxability applies to income tax and the proportional tax is applied to other taxes like customs duty, VAT, excise duty, service tax, and wealth tax. Within income tax, certain types of income, such as lottery income, long-term capital gain, and short-term capital gain in some cases, are taxed under proportional taxation. Companies and firms are subject to proportional taxation, while individuals and cooperative societies are subject to progressive taxation. The tax structure in India is divided into three tiers, with the Union government having the power to levy taxes like income tax, customs duties, excise duties, and taxes on sales and services. State

governments impose various taxes, including state excise, sales tax, stamp duty, land revenue, entertainment tax, and professions tax. Taxes such as octroi, taxes on properties, taxes on markets, and tax/user charges for utilities are levied by local bodies. A comprehensive income tax, intricate customs charges, intricate indirect taxes, and tax incentives are all included in the Indian tax system. However, India's federal republic structure, combined with its intricate local government, results in an unbalanced tax system that needs to be simplified for the various economic sectors.

#### III. Major Tax reforms in India and their impact on the economy

##### i. Introduction of VAT and history of Tax Reforms

India's tax reform efforts started in the mid-1980s and continued with the creation of a Tax Reform committee in 1991 under Prof. Raja Chelliah. The committee proposed broadening the tax base, reducing corporate tax rates and marginal tax rates for individual categories, introducing a value-added tax (VAT) system for services, and simplifying laws and procedures. The recommendations were partially implemented at the central level but not at the state level. The Task Force on tax reforms, headed by V. Kelkar in 2002, proposed more comprehensive reforms, including a cut in corporate tax rates, simplifying procedures, and implementing a destination-based VAT.

##### ii. Direct Tax Reforms in India

According to data released by CBDT, Department of Revenue, Ministry of Finance, Government of India, only 5% of individuals filed their income tax returns in 2016-2017, and many have declared their earnings below the tax threshold, leading to over half of the tax returns having zero tax liability. However, the government has taken steps to increase the number of taxpayers, resulting in a 70.86% increase in electronic tax returns filed. Despite these measures, the public perception of the tax bureaucracy as corrupt and inefficient still prevails. The government must undertake stricter legal and administrative reforms to

<sup>2</sup> Ahluwalia, S. Montek, 'India's Economic Reforms: Achievement and Next Steps'. *Asian Economic Policy Review* (2018) 14, 1-17, doi: 10.1111/aepr.12239

tackle tax evasion within the country and reassess its direct tax policy framework to move towards a progressive tax regime.

### iii. Impact of GST Tax reform

The article highlights the significance of the Goods and Services Tax (GST) in India as a significant tax reform. GST is a comprehensive tax on the manufacturing, sales, and consumption of goods and services based on the value-added principle with a continuous chain of benefits from the producer to the end user. India has adopted a dual GST system. GST is expected to simplify the indirect tax structure in India and have far-reaching impacts on businesses in all sectors of the economy. However, the transitional process may have some discrepancies, but it will lead India on the path of planned economic development. The article concludes that GST will be a milestone in years to come, appreciated nationally and globally as foolproof one-tax machinery in any country. The initiative taken by the state and central government is appreciated for striking a consensus after breaking a decade-long deadlock.

### Conclusion

The tax reforms in India have had a significant impact on the economy, particularly on the business and investment climate. The GST has improved the ease of business in India, making it easier for companies to operate across state borders. The simplified tax structure has also made it easier for businesses to comply with tax laws, reducing the risk of tax evasion and fraud. In conclusion, tax design and tax reforms play a crucial role in the economic development of a country. India's recent tax reforms, particularly the introduction of the GST, have positively impacted the economy by improving the ease of doing business and increasing tax revenue. However, more work must be done to ensure that the tax system is transparent, fair, and equitable for all taxpayers.

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