The Impact of Taxation System on Economic Growth in India

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Abstract— Indian taxing system is one of the most important sources of revenue to the Government and at the same time one of the deciding parameter for economic growth. Whereas direct tax impacts directly the disposable income, the indirect tax impacts the prices of goods and services in the market. The basic objective of this article is to evaluate the impact of both direct and indirect taxes on economic growth of India. Today Indian taxing system is going a revolutionary change owing to spreading the wings of Indian business into global market. Indian Government is paying its full attention to liberalize the taxing system and at the same time closing the loopholes to disable the intruders to evade the taxing system so as to enlarge the revenue to Government exchequer and flourish the overall business scene. Broadly taxing system may be classified into three parts:

- Progressive taxation implies a taxing system where tax rate increases with increase in income, thus if a person has higher income, he will bear more tax burden due to increased tax rate than person having lesser income.
- Regressive taxation means a taxing system where tax rate reduces with increase in income and thus a person having lesser income faces lesser tax burden due to facing lesser tax rates.
- Proportion tax means a taxing system of charging tax on a fixed proportion irrespective of level of amount on which tax is to be levied. Thus, the same tax rate applies to different persons having different taxable amounts. Tax may be levied on natural persons like individual, Hindu undivided family artificial entities like Firm, association of persons, company, society etc. and also on goods and services. Thus, another classification of tax we found into direct tax and indirect tax.
- Direct tax means a type of tax which is paid by a person directly to the Government. For example income tax and wealth tax in India.
- Indirect tax means tax on goods and services which are paid by a person to the producer, seller or service provider who is liable to pay the same to the account of Government. For example customs duty, excise duty, VAT, service tax, entertainment tax etc. in India. Now a modern system of taxing all goods and services — after introducing goods and services tax(GST), It replaced all existing enactments relating to goods and services.

Keywords: Economic Growth in India, GST, VAT

I. TAXING SYSTEM IN INDIA

In India, progressive and proportional taxing systems are followed. In Indian tax law, slab wise taxability arises somewhat for income tax while proportional tax is applicable for GST. Further under income tax, lottery income, long term capital gain, and in some cases short term capital gain is taxed under proportional taxation system. Again the income of assesses such as for companies, firms etc. proportional taxation system is applied while for individual and cooperative society, progressive taxation system is followed. Among direct tax only three types of taxes are in existence today, namely income tax, wealth tax and Corporate tax

- Income tax: Under Indian income tax law both flat rate (proportional tax) and slab rate (progressive tax) applies. Tax is computed on total income. On lottery income, long term capital gain, and in some cases short term capital gain is taxed under proportional taxation system. Again the income of assesses such as for companies, firms etc. proportional taxation system is applied while for individual and cooperative society, progressive taxation system is followed. *Wealth tax: wealth tax is levied at 1% on the net wealth of individual, Hindu undivided family and company if net wealth exceeds Rs.30 lakhs on the valuation date. It is payable in every assessment year based on valuation of net wealth on the respective valuation dates. Valuation date means last day of the corresponding previous year relating to each assessment year. Net wealth is computed as the difference between value of assets and the value of liabilities. Assets include House, Motor car, Jewellery, Urban land, Cash in hand and yatch, boat and air craft.
- Corporate tax: Levied on companies who exist as separate entities from their shareholder. Foreign companies are taxed on income that arises, or is deemed to arise, in India. It's charged on royalties, interest, gains from sale of capital assets located in India, fees for technical services and dividends. Includes Minimum Alternative Tax(MAT) which was introduced to bring Zero Tax Companies Act. Includes Dividend Distribution Tax(DTT) which is a tax levied on any amount declared, distributed or paid as dividend by any domestic company. International companies are exempt from this tax. Includes Securities Transaction (STT) which is a tax levied on taxable securities transaction. There is not surcharge applicable on this.

II. THE IMPACT OF DIRECT TAX ON ECONOMIC GROWTH

The direct tax is one of the important sources of government revenue. Further it also impacts directly the disposable income of individuals. If direct tax rate is increased by the Government, people start saving for investment purposes. Due to this behavior of individual's income generation process of economy is hampered. Particularly this is true for luxury commodities. This decreases the production of luxury commodities in the economy and as a result also adversely affects the GDP and standards of living. However on the positive sides, if proper deductions are allowed based on investments, it leads to capital formation in the country. Thus, broadly following are the positive sides of direct taxes on the economic growth:

- *Better capital formation
- Inducement of saving and investment
- Surety of Government's revenue growth
- Increase in planned expenditure of government

- Decrease in inflation rate due to lesser availability of disposable income to persons
- Timely availability of revenue to the Government

III. INDIRECT TAXES

After major reforms in Indian Indirect tax system the main tax is GST although some other taxes is also exist other than GST like.. *Basic Customs Duty *Central Excise and VAT on petroleum products *State taxes on alcohol for human consumption *Electricity Duties *Stamp Duty *Securities Transaction Tax *Property tax and other taxes to municipalities *Toll tax

A. GST Concept, Classification and Rates

GST(Goods and Service Tax) is applicable on supply of goods and service. It replaced the current taxes of exise, VAT and service tax. In past times there different VAT laws in different states. Most businesses had to pay and comply with three different tax. GST brings uniform taxation across the country and allows full tax credit from the procurement of inputs and capital goods which can later be set off against GST output liability. Current GST system makes equal balance to the big enterprises as well as SMEs.

GST is classified into three types:

- CGST- Central GST
- SGST- State GST
- IGST- Integrated GST

Tax Rates	Products
5%	Household necessities such as edible oil, sugar, spices, tea, and coffee(except instant) are included, Coal, Mishti/Mithai(Indian Sweet) and Life-Saving drugs are also covered under this GST slab.
12%	This includes computers and processed food.
18%	Hair Oil, toothpaste and soaps, capital goods and industrial intermediaries are covered in this slab.
28%	Luxury items such as small cars, consumers durables like AC and Refrigerators, Premium Cars, Cigarettes and Aerated drinks, High-end motorcycle are included here.

B. Impact Of Indirect Tax On Economic Growth

Since the burden of Indirect taxes directly fall on the consumers, it directly impacts the cost of goods and services. Thus, indirect tax increases the efficiency of the producers, since to maintain their demand they will have to put their full efforts towards cost cutting measures. Further, this effort of producers also brings proper utilization of resources in the economy. The consumers are at freedom to select products at their choice, thus healthy competition also grows in the economy. Thus, broadly following are the positive sides of indirect taxes on the economic growth:

- Better utilization of resources
- Increase in efficiency of producers
- Growth of healthy competition in the market
- More freedom of choice to the consumers
- Increase in demand for luxury goods
- Increase in standard of living of people

C. Need Of Direct Tax Reforms

GST has brought in a structural change in the indirect tax system in India. Continuous improvements in the structure, IT, administration and review systems in the GST through the GST council will certainly improve the current construct and lift the economy up in the years ahead. What is needed now is a similar reforms on the direct tax front. It is time tp revamp the Income Tax Act 1944. Over time, cosmetic changes, complications, poor tax administration and a complex law crept in.

What is needed is a simple, easy-to-understand but effective direct tax law. A few key areas need focus: clarity is required as to whether income tax is on gross income or net income. In other words, is the objective of income tax to tax gross income or income after savings, investments and consumption. The tax base needs to be widened. Only 1.5% of our 130 crore people pay Income Tax and only 30000 people earn more than Rs 1 crore per annum. A good 90% of taxpayers contribute to only 23% pf tax revenue. A large-scale exclusion of the population in paying Income tax is seen. Predictably, the base has shrunk from 2.7 crore in FY’03 to 2 crore in FY’19. While salaried persons in the formal sector dutifully pay income tax, there is large-scale evasion from informal sector, traders etc. This needs plugging.

D. Suggestions

- High rates are a recipe for low tax compliance.
- A lower rate for lower incomes and higher incomes will ensure better balance.
- The threshold for Income Tax needs to be revised periodically to counter the effects of inflation.
- A plethora of exemptions and deductions, adding to litigation on these, needs to be removed.
- For individuals, there should be simple formula for net income from all sources is Rs 100, allow 35% for savings, 32.5% of gross income should be taxable.
- For corporates, the calculation is as follows. For 100 of profit before tax, add book depreciation of 10%. Limit 35 % for investments in assets for future business growth. Hence income chargeable to tax is Rs 71.5.
- For individuals, those earning below Rs 5 lakh need not be taxed. Those between this floor and Rs 10 lakh should be taxed at 5 %, while income between Rs 10 lakh and Rs 1 crore should be taxed at 10 %.
- The next slab till Rs 10 crore should see 15 % tax. Anything above that would be taxed at 20 %.
- For corporates , rate should be 10% up to Rs 100 crore of chargeable Income and 15% between that floor and Rs 500 crore.The next slab up to Rs 1000 crore should be taxed 20 %. Those above Rs 1000 crore should be taxed at 25 %.
- Once audited accounts are as per accouts are as per accounting standards, tax authorities should not have any discretion to review the basis of accounting. This will ensure avoidance of unnecessary legal disputes.

IV. CONCLUSION

Both Direct and Indirect taxes are important for our country as they are linked with overall economy. Both are collected by the central and respective state governments according to the type of tax levied and are important for the government as well as growth perspective of the country. However taxing of both direct and indirect is indispensable in modern public finance. In countries like India having people with varied economic backgrounds, the Government should more focus on direct taxes rather than indirect taxes by ensuring proper administration of direct taxes to eradicate tax avoidance and tax evasion. It concluded that the contribution of central direct tax to total central tax revenue has increased year by year whereas central indirect tax contribution has decreased taxation system playing important role in the growth of economic and progressive growth are possible due to both type of taxes.

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