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CHALLENGES IN THE CURRENT INDIAN TAX REGIME

AUTHORED BY - KALYANI ROY & VIJAYA GUPTA

INTRODUCTION

The concept of tax is not new. It has existed since time immemorial in different forms and nature and has evolved slowly to match the socio-economic needs of the people and the societies. We see the presence of taxes across various jurisprudences across different time periods. The presence of tax can be evident in various civilizations that have existed, such as the Mesopotamia and the Egypt civilization to Athens and Rome where the taxes in were not in the form of monetary or fiscal manner, but rather in the form of goods and services, example crops, labor, animals, etc. that were given to the King who would use these form of taxes for the betterment of the people and his kingdom and in return would provide protection, employment, etc.

Nowadays, we can see a drastic change in the way this generation perceives the meaning of taxes. In India and most other countries, Tax is a form of compulsory extraction of fee or charge, only in the form of money, levied on the individual or rather the residents of the country. This extraction of money that is charged by the government based on various factors and criteria is in the end used for the welfare and benefit of the people themselves. This tax levied by the government aids in the development of the nation, upliftment of the society, etc.

As we know that post-Independence, India adopted the ideology of a Welfare State, which means a State whose functions could not be curbed to mere sovereign functions of the government, such as defense, administration of justice, etc. but was expanded to include a wide range and categories of other functions, i.e., non-sovereign functions also, such as better infrastructure, healthcare, education, etc. Thus, with the increase in the functions of the State, the Government of India needed more funds and capital to carry on and discharge efficiently the duties and obligations of the State. Just like the banks charge interest on the loans given to the customer, in a similar way here we can say that the taxes are also levied by the government on the people against the facilities that are being provided to them, e.g., better roads, better healthcare infrastructure, better welfare schemes, etc.

Thus, the money collected in the form of taxes aids in resource allocation, income redistribution, increasing economic stability, and decreasing inequality in the society by collecting it from people eligible to pay taxes and then redeploying the capital and the resources in more efficient places, which is the need of the hour specially in resource constraint nations such as India. Hence, due to these reasons, the nature of tax which has developed over a long jurisprudence can be narrowed down to a compulsory extraction of money which may or may not be quid pro quo, as has been held finally in the case of *Jalkal Vibhag Nagar Nigam v. Pradeshiya Industrial and Investment Corporation*.¹

Thus, the monetary nature of tax which may create a burden on the people makes the interpretation of the tax legislatures very strict in nature and in favor of the taxpayer, who cannot be taxed without the presence of a law passed by the Parliament.

Therefore, in simpler terms, we can say that every economy owes its development, stability, and sustainability to the money of the taxpayers in the form of tax. Hence, as the Tax is a crucial part of any economy, the nations must persistently work on improving the tax regime and tax structure in their country, thus for the same reason, the researchers in this paper have tried to analyze and highlight the various challenges or lacunas that is present in the current tax regime in India and have also suggested some ways in which such loopholes or lacunas can be filled.

In order to do the same, the researchers would be dealing with two research questions which would be followed by a conclusion and suggestions for the following problems.

Chapter 1- The current tax regime presents in India

Chapter 2- The challenges in the current tax regime

¹ *Jalkal Vibhag Nagar Nigam v. Pradeshiya Industrial and Investment Corporation*, 2021 SCC OnLine SC 960.

CHAPTER 1

Taxes under the Indian tax regime can be broadly classified into two categories i.e., Direct Tax and Indirect Tax. The theories that could be involved and form the basis of this classification are first, pinching the taxpayer, and secondly, the incident and impact theory.

Direct tax When an individual directly pays taxes to the government, it is known as direct taxes. Under the direct tax, the burden of tax levied on an individual cannot be shifted, who pays such taxes proportional to the income he earns, thus making direct taxes progressive in nature, i.e., higher taxes levied on higher income. Therefore, as the burden to pay the tax cannot be shifted into direct tax, thus the incidence and impact fall on the same person.

The different types of direct taxes are:

Income Tax: This tax is levied on the income of an individual and HUF and is regulated by the Income Tax Act, 1961. An individual has to pay the tax as per the slabs stated by the Central Government every year in the annual budget.

Capital Gains Tax: An individual has to pay capital gains tax when he is incurring profits from the sale of a capital asset. There are two types of capital gains tax long-term capital gain and short-term capital gain which are levied on the capital assets held for more than 36 months and on capital assets that are held for less than 36 months respectively.

Corporation Tax: This tax is also a kind of income tax because it is levied on the income of the companies and corporations, either registered in foreign or in India. Corporations have to pay taxes as per the tax slabs stated by the Government. This tax is also known as a surcharge.²

Indirect- Taxes which are levied on the goods and services This tax is originally levied on the sellers or manufacturers but is shifted on the consumers who would be indirectly burdened to pay the taxes. Indirect tax is regressive in nature because it is not levied in proportion to the income of the individual.

² Aashika Jain, Taxation in India: Direct Taxes You Need To Know About, Forbes Advisor, (Dec 18, 2020, 7:17 AM), available at <https://www.forbes.com/advisor/in/tax/direct-taxes-you-need-to-know-about/>, (last visited on May 7, 2022).

The Indirect taxes currently includes:

Goods and Service Taxes (GST): Before GST there were various indirect taxes such as VAT, Service Tax, Entertainment tax, etc. which have now been replaced by one tax i.e., GST. This tax is levied on the manufacture, sale and consumption of goods and services. There are three types of GST currently levied in India SGST and IGST.

Custom Duty: This tax is imposed when any good is exported or imported into India.

CHAPTER 2

On one hand, though every nation wants to become a developed nation with the greatest standards of living, best facilities, and best infrastructures, on the other, the government should make sure that the scheme or strategy deployed by them in order to achieve this goal must not become burdensome on the innocent taxpayers. Therefore, through a close analysis of the current tax regime, we can still find various loopholes that are present in the tax structure, and which need to be improved in order to make the tax structure, efficient, effective, and most importantly taxpayer-friendly.

Some of the loopholes or lacunas in the current tax regime are as follows-

1. According to the current tax structure, the taxpayer's base of direct taxes is very small. In addition to this, the government has kept the tax slabs and tax rates very high, which in turn results in disincentivizing the people from paying taxes. Thus, as a result of this, even when the tax rates are huge which should allow the government to collect huge taxes, in reality, this is not the case as high tax rates lead to a greater number of tax evasion by people, hence resulting in low yield of revenue.³
2. Further, these huge tax rates act as a huge disincentive for the people to pay the taxes, who thus resort to unfair means of not paying taxes by tax evasion, which is a crime. Thus, these huge tax rates lead to higher tax evasion. Also, the tax evaded ultimately results in black money, which makes the country more corrupt and bad in the eyes of other nations.⁴

³ 8 Major Defects in the Tax Structure of India, Economics Discussion, available at <https://www.economicdiscussion.net/taxes/defects/8-major-defects-in-the-tax-structure-of-india/12917>, (last visited on May 7, 2022).

⁴ Vaisakhi Muddana, What are the Problems in Tax Structure and Administration In India, iPleaders Blog, (December 30, 2016), available at <https://blog.iplayers.in/problems-in-tax-structure-and-administration-india/>, (last visited on May 7, 2022).

3. Because the revenue or capital yielded in the form of taxes is low, which may not be enough for the government to carry on the essential functions of the State, as a result of this the country may become a victim of under-development, poverty, unemployment, poor healthcare, and educational infrastructure, etc. further, the government may as a result of the low and insufficient funds collected in the form of taxes further increase the tax rates, resulting into a further increased burden of the innocent taxpayers.
4. India is an agricultural country, which means that the maximum population of India are in the Agriculture sector, yet one of the major drawback or loopholes in the tax laws in India is that even though the maximum income generated in India is in the form of agricultural income, yet at the same time the agricultural income in India is not subject to taxes. This is a major drawback because this automatically removes more than half of the population from paying the taxes. In addition to this, this exemption which saves the agricultural income from being subjected to the taxes is also discriminatory in nature. The reason for this is that many rich owners of agricultural land are excluded from paying taxes as compared to the other working-class or middle-class people who become the victims of high taxes.⁵
5. A detailed analysis shows that it is the indirect tax in India that forms the greater part of the revenue generated by the government in the form of taxes. Although the problem of multiplicity of indirect taxes has been to a huge extent done away with by the introduction of GST, still the problem of ambiguity continues as a result of the various rates of tax present and the huge number of classifications that exist.

Hence, in reality, the GST laws which were introduced to do away which the multiplicity and complexity in the indirect tax regime have actually failed to accomplish this objective in furtherance of increasing the cost of compliance for the same.

6. The nature of Indirect tax is regressive in nature and actually acts against the interest of the poor as they have to pay a huge part of their small portions of earnings as a form of indirect tax on the purchase of even every day and essential goods and services. Thus, this increases the burden on the poorer and disadvantaged sections of the society who have to

⁵ Shruti Rajagopalan, Rethinking India's Tax System, Livemint, (Dec 26, 2017, 04:58 AM), available at <https://www.livemint.com/Opinion/z2DURCdrbtLjCPnutKs3gJ/Rethinking-Indias-tax-system.html>, (last visited on May 7, 2022).

pay taxes even in order to consume the most basic and essential goods or services which per se results in inequality. This is because this indirect type of tax, which is regressive in nature results in charging the same tax to everyone, irrespective of their income, and without creating reasonable classifications amongst the taxpayers, hence can be said to be violative of Art.14 of the Constitution.⁶

7. The indirect tax which forms the major source of revenue in India has a huge disadvantage attached to it. The issue with such indirect tax is the cascading effect it causes. This means that every stage that the product passes, like the stage of production, transportation, etc. results in the addition in the cost of the product, which in the end is passed to the end consumer, who bears the burden of it in the form of indirect tax on the goods or services consumed.
8. The high tax rates act as a great disincentive from doing business in India, which in turn results in various other socio-economic problems such as increased unemployment, decrease in investment by creditors, and other businesses who do not have enough reason to invest in such corporations due to the fewer profits incurred as a result of the high corporate taxes.
9. The poor financial education in the people, especially the poor and the disadvantaged group further results in increasing the inequality and disparity between the rich and the poor. This is because, the rich and the educated lot are using and exploiting the loopholes present in the current tax laws in their interest by paying lesser taxes, i.e., tax avoidance. While on the other hand, the poor and the uneducated lot are becoming victims of the high tax rates levied by the government.

CONCLUSION

An ideal tax regime system should treat its taxpayers with fairness, justice, and equity. Though the current tax laws in India offer various benefits to the taxpayers yet to some extent it creates a burden on them. Thus, it becomes absolutely necessary to build a tax structure that not only looks after its taxpayers and preserves their interest but also creates a system in which tax paying is morality rather than a choice. In order to build such a system, there is a need to primarily fill up

⁶ Ibid.

the lacunas that are present in the current Indian tax regime and has also been highlighted by the researchers in this research paper.

Thus, the various measures that could be adopted in the current tax regime to make it more transparent, smoother, efficient, effective, and at the same time burden-free and taxpayer-friendly could be-

1. India which currently relies barely on property tax should start relying more on property tax. The reason for the same is that this would help the government to increase the revenue that is being generated from the direct taxes. Further, the property tax would be more economic friendly and progressive in nature because the property being immovable, is difficult to hide, unlike income, therefore making it difficult to evade property taxes.⁷
2. Government should make persistent efforts to decrease the income tax rates to a large extent. This would help India in generating more yields in the form of capital as the lower tax rates would not act as a disincentive on the people who would therefore resort less to unfair means like tax evasion.
3. The legislation dealing with tax should be amended to form a more robust tax framework with much higher and stricter penalties for tax evasion, so as to deter the people from resorting to such illegal means. More comprehensive tax laws should be formulated to remove ambiguity from the current tax laws, increase uniformity, increase compliance, and decrease litigation. Therefore, the formation of stricter as well as taxpayer-friendly laws would in turn result in higher revenue for the government in the form of taxes, even at lower tax rates.⁸
4. The absence of products such as petroleum, tobacco, etc. in the current GST system creates ambiguity in the tax rates as different States can charge different prices for the same. Hence, these products which are so high in consumption must be brought within the ambit of uniform GST so as to deter the creation of an illegal market for them and to increase accountability.⁹

⁷ Supra Note 5.

⁸ ET Bureau, Complex Tax System Big Reason for Indian Startups' Exodus, The Economic Times, (Dec 13, 2021, 05:49 PM), available at <https://economictimes.indiatimes.com/tech/startups/complex-tax-system-big-reason-for-indian-startups-exodus-report/articleshow/88246259.cms?from=mdr>, (last visited on May 7, 2022).

⁹ Shantanu Nandan and Suman Layak, ET Bureau, GST: The Challenges Before India's Largest Indirect Tax Reform, (Sep 29, 2019, 11:18 AM) available at <https://economictimes.indiatimes.com/news/economy/policy/gst-the->

5. As mentioned earlier, the GST was formulated in order to ease the complexity of multiple taxes and to provide clarity for the same but the current GST system with a high number of classifications and different rates fails to accomplish the objective of it. Thus, GST laws need to be reframed in order to simplify the rules regarding the same and to bring uniformity.¹⁰
6. India should start imposing inheritance tax like other nations such as the USA, and the UK, which can be a sure shot method to collect revenue in the form of taxes from the riches without burdening the poorer.
7. Post Covid it is absolutely necessary that the government reforms its taxing policies and structure in order to provide a fair chance to the taxpayers to bounce back from the increased burden created due to the pandemic and the lockdown. Thus, there is a need for the government to fix its tax structure to achieve social and economic justice in society.¹¹

Therefore, as earlier stated, every nation should make persistent efforts to become a holistic State, with a greater standard of living, good healthcare and educational infrastructure, better welfare scheme, etc., but the same can only be done when the government has enough funds. Hence, for the development of the nation, it is necessary for the government to collect taxes from the people. Hence, what the government needs to ensure in this process is that such collection should not be done at the absolute disadvantage of the people. The government and the legislature need to imbibe the perspective that the development of the nation is owed to the money of the taxpayer. Hence, tax laws and regulations should be formed and amended in order to equally look after the interest of these innocent taxpayers.

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¹⁰ Pravas Rajan Mishra, GST has increased India's Reliance on Indirect Taxes, Hurting The Poor, (Jul 14, 2021), available at <https://thewire.in/economy/gst-india-indirected-taxes-inequality>, (last visited on May 7, 2022).

¹¹ Christophe Jaffrelot, Ustav Shah, Centre's reliance on Indirect Tax Revenue, Pro-rich policy, Has Deprived Govt Resources During COVID Crisis, The Indian Express, (August 11, 2020, 11:56 AM) available at <https://indianexpress.com/article/opinion/columns/india-taxation-policy-fiscal-deficit-covid-impact-on-economy-indirect-tax-revenue-6549290/>, (last visited on May 7, 2022).