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A STUDY OF DIRECT TAX REFORMS IN INDIA - SINCE 1991

Dr. Chetna Bisht[1] and Diksha Chauhan[2]
Associate Professor, Economics, D.B.S(P.G.) College, Dehradun, Uttarakhand.

ABSTRACT:

India launched various programme of Economic reforms in 1990's.Reforms were primarily undertaken in response to fiscal crisis it faced in 1990's and main aim of these reforms was to attained macroeconomic stability. To achieve stability in economy it becomes necessary to re-examine the structure of tax system.

Therefore since 1991 a number of committees have been constituted from time to time to give recommendation for existing tax structures. In this context this paper makes an attempt to study various policy initiatives taken so far in the area of direct tax reforms and most important to analyse the impact of these reforms on collection of Direct taxes.

KEYWORDS*: Direct tax reforms, Income tax, corporation tax, fiscal crisis.*

1. INTRODUCTION:

In 1980 and 1990 many developing countries implemented a serial of economic reforms. During these decades, re-assessment of role of government ineconomy took place, which leads to shift in favor of assigning a greater role to the private sector including foreign enterprises. Thisnecessarily required re- examination of the structure of the tax system. Thestimulus for reform in thetax system came primarily from the need to raise additional revenues to deal with the problem of continuing and in some case, rising deficits,but since the structural reform of real sector of economy was also being attempted,efficiency consideration were also important cause (chelliah 1996).Whileit was felt that there is a need toraise revenue to fund activities of the government economists were also tasked with figuring out how to design a revenue system that the both efficient and equitable (Ulbrich2003).

India too launched Economic reforms in1990's. Reforms were primarily undertaken in response to fiscal crisis it faced in 1991 and the main aim was to attained macro-economic stability. By mid 1991, India foreign exchange revenue had declined to just two weeks of import coverage. Public debt had reached monsters level. The debt service burden rose from 10 percent of current account receipt and 15 percent of export earnings in 1980-81to 22 percent of current account receipts and 30.5 of export earnings in 1990-91.Rising fiscal deficits and monetization of a substantial portion of it led to inflationary pressures and growing deficit in the current account of balance of paymentswhich becomes prime mover for the change.

1.1Tax System In India

India has a three-tier federal structure (the Union Government, the state government and the Urban/Rural local bodies). The power of taxes and duties is divided between the union government and state government in accordance with the provision of India constitution. The tax system in India comprises of direct taxes as well as indirect taxes. Except for land revenue and the agriculture income tax all other direct taxes are levied and collected by the federal level and central board of direct taxes (CBDT) has been given responsibility of all matter relating to various direct taxes in India, central board derives its authority from central board of revenue act 1963.

1.2 TYPES OF DIRECT TAX

In India, taxes levied on income and wealth by the central government. Though the state governments have the power to levy a tax on agriculture income, yet in practice this tax has not developed as the major source of resource of state, the central Government levies a number of taxes on income and wealth of which from the revenue point of view only personal Income tax and corporation tax are important.

Personal Income tax is levied on income of individual, Hindu undivided families, unregistered firms and other association of people by the central government. The Income tax does not fall on all people but only on those people who are better off. It is based on the principle of 'ability to pay' that is, those who can pay more should pay more to the Government. For taxation purpose income from all sources is added. Like all other countries, India has progressive income tax.

Corporation tax is levied on the income of registered companies and corporation. These taxes are based on the income of registered companies and firm in country (it can be national, multinational or foreign). National companies in India are taxed on the basis of their aggregate income, irrespective of its source and origin. Whereas foreign companies are taxed only on Income that arises from operations carried out in India.

2. OBJECTIVE AND RESEARCH METHODOLY OF THE STUDY

India undertook major economic reforms in1990s. In addition to structural reforms,major reforms in taxation area were also undertaken with the policy guidelines framed by the committee headed by Dr Raja J Chelliah. A number of more committees have been constituted from time to time to suggest changes in the existing tax structure. The main objective of these changes has been to enhance tax revenue by enlarging tax base, encouraging voluntary tax compliance and simplifying procedural rules. In this context, it is important to study various policy initiatives taken so far in the area of direct tax reforms and most important to analyse the impact of Direct tax reforms on collection of direct taxes.

The study is mainly based on the secondary data which is covered from the time period of the year from 1991-2018. However, many sources of data have been taken to prepare a set of data as the requirement of the study. The secondary data source which is published by reserve bank of India, consulted for the study. Theother sourceincludes India Public Finance, Annual budget of Government, All India Income tax statistics, Report on Direct taxes and various reports of the finance commission, andresearch journals.

In backdrop of above discussion to study the impact of direct tax reforms on collection of direct taxes following indicators are analysed-

A. Direct tax revenue as percentage of gross tax revenue
B. Direct tax revenue as the percentage of gross domestic product at current market price
C. Comparison of trends in direct tax revenue

3. TAX REFORMS IN INDIA

Restricting the tax system at federal level was central to the entire process of economic reforms. Direct tax reforms at federal level formed key component of wider reforms in fiscal and economic sector. Like in other developing countries, in India also has the tax reforms aimed at correcting fixed imbalanced, (Ahmed and Stern 1991). In India post- tax reform were, clearly in response to fiscal difficulties that emerged in late eighties and reached crisis proportion 1991.

The Government of India had realized that restructuring of the complicated tax structure was required to solve the problem of fiscal crisis through enhancing revenue and for the transformation of the economy. Therefore, since 1991, there have been a number of attempts at reforming direct tax at the Union level to simplify and rationalise the tax system. The Tax Reform Committee (TRC) with Raja Chelliah as the Chairman appointed immediately after economic reforms were initiated made far reaching recommendations for the simplification and rationalisation of both direct and indirect taxes (India, 1991, 1993). These recommendations were implemented during the period 1991-95 and the direction of reforms set in these recommendations continued thereafter. A comprehensive review of the tax system was made again in 2003-04, in the two reports chaired by Vijay Kelkar on Direct and Indirect taxes (India, 2003 and 2003a). In addition, reviews have been done on specified taxes such as the Report of the Expert Group on Taxation of Services (India, 2001), Report of the Advisory Group on Tax Policy and tax administration for the Tenth Plan (India, 2001a). More recently, Tax Administrative Reform Committee chaired by ParthasarathiShome, in a series of four reports, has comprehensively dealt with the reform of tax administration including revenue forecasting and research (India, 2014, 2015).

3.1 DIRECT TAX REFORMS IN INDIA

In this section we will discuss measures that have been taken by Indian government to enhance tax revenue by enlarging tax base, encouraging voluntary tax compliance and simplifying procedural rules in various budgets since 1991.

- The number of tax slabs for Income tax was reduced.
- The maximum marginal rate of Income tax was also reduced. Presently it is only 30 percent but in eighties it was more than 90 percent.
- Wealth tax on productive assets was abolished.
- Corporate tax was also gradually reduced
- Many initiativeswere taken in every budget to widen the tax base. Forexample, 'one by six 'criteria
- MAT, (Minimum Alternative Tax) was imposed on several zero tax companies.
- In 2000-01 Non-agricultural income of farm houses madetaxable.
- In 1999-2000 Income earned by way of dividend and by way of long-term capital gains from global depository receipts allotted to the resident employees of the Indian company engaged in information, technology, software and services to be taxed at the concessional rate of 10 percent.
- To increase tax compliance strengthening of Information system through TIN.
- Tax Administrative measures have been taken to improve reporting and widening tax base for example
  - Introduction of a simple one-page Tax payer friendly return form called 'SARAL.
  - Making it obligatory for assesses to quote their PAN or GIR number in respect of certain high value transaction.
- Introductionof a new scheme called "KAR VIVAD SAMADHAN SCHEME' to recover the money locked in litigation both in direct and indirect
- To bring black money in to the tax system many steps were taken by the government for example
  - Voluntary disclosure scheme in 1997-98
  - In 2016-17 the domestic tax payer can declare their undisclosed income by paying 30 percent tax,7.5 percent surcharge and 7.5percent penalty (which is 45 percent of total undisclosed income)
  - In 2016-17, Penalty rates to be 50 percent of tax in the case of underreporting of Income and 20 percent when it is misreporting facts.
- To increase tax revenue several tax exemptions were removed for example
  - In 2002-03 exemptions on casual and non-recurring receipts{10(3)}, exchange risk premium{1)(14A)},interest on notified capital investment bonds and and bonds purchased in foreign currency by NRI{10(15)}, income of local authorities other than panchayats and municipalities{10(23)},income of marketing authorities{10(23A)} were removed.
  - In 2008-09 Banking cash transaction (BCT) has being withdrawn.

3.2 IMPACT OF REFORMS ON COLLECTION OF DIRECT TAXES

The impact of reforms on collection of direct taxes has been measured in terms of the following indicators.

(I) Direct Tax Receipts
(II) Direct Tax Revenue as a percentage of gross tax revenue
(III) Direct Tax Revenue as a percentage of gross domestic product at current market prices
(IV) Comparison of trends in tax GDP Ratio

(I) DIRECT TAX RECEIPTS

The following table shows the direct tax receipts under the period of study

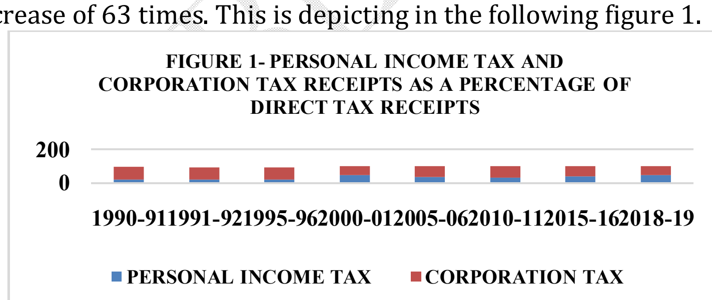
Table1- DIRECT TAX RECEIPTS

YEAR	DIRECT TAX	PERSONAL INCOME TAX	CORPORATION TAX
1990-91	6903	1250(18.10)	5335(77.28)
19991-92	10103	1627(16.10)	7823(77.72)
1995-96	22287	4318(19.37)	16487(73.97)
2005-06	120692	45238(37.48)	75187(62.29)
2010-11	313501	102441(32.67)	209115(66.70)
2015-16	449296	172748(38.44)	275917(61.41)
2018-19	732892	333173(45.46)	399712(54.53)

Source: RBIhandbook of Statistics of Indian economy

Note: Figure in parenthesis shows the Income tax receipt and Corporation tax receipt as a percentage of total direct receipts

Analyse of above table 1 reveals thatthere is constant increase in the value of direct tax receipts it has grown from 6903 cr in 1990-91 to Rs 732892 cr in 2018-19 showing a tremendous increase of more than 21 times, for the same period ,corporation tax receipts grown from 5335 cr rupees to399712 registering an overall increase of 63 times. This is depicting in the following figure 1.



Source: RBI handbook of statistics of Indian Economy

(II) DIRECT TAX REVENUE AS A PERCENTAGE OF GROSS TAX REVENUE

Total direct tax receipt and its major component viz,Personal Income Tax and Corporation tax have been analysed in following table -2 as percentage of gross tax revenue.

Table-2 DIRECT TAX REVENUE AS A PERCENTAGE OF GROSS TAX REVENUE

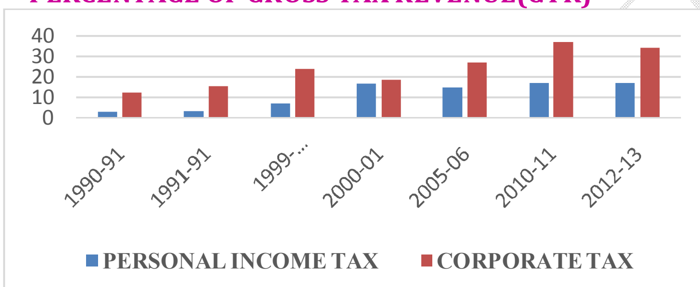
YEAR	PERSONAL INCOME TAX	CORPORATE TAX	TOTAL DIRECT TAX
1990-91	2.91	12.41	16.06
1991-92	3.25	15.68	20.18
1995-96	5.02	20.12	27.20
1999-2000	7.11	23.93	32.30
2000-01	16.86	18.42	35.80
2005-06	15.03	27.07	43.0
2010-11	17.05	37.07	52.03
2012-13	17.06	34.06	54.09

Source:Economic Survey

As evident from the table 2 the personal Income tax revenue as a percentage of gross tax revenue has overall shown a tendency to increase in spite of fluctuation from time to time during the period under review. It has increase from 2.91 percent in the year 1990-91 to 17.06 percent in 2012-13. But in year 2000-01 it increases tremendously to 16.86 percent from 7.11 percent in 1999-2000.On the other hand corporation tax receipts increased from 12.41 percent in 1990-91 to 34.6 percent in 2012-13. This is depicting in the figure 2.

As a result of increase in both of its major component that is Personal income tax and corporation tax the total direct tax revenue has also increased as a percentage of direct tax revenue. It has increased from 16.06 percent in the year 1990-91 to 54.09 percent in year 2012-13.

FIGURE 2 -INCOME TAX AND CORPORATION TAX REVENUE AS A PERCENTAGE OF GROSS TAX REVENUE(GTR)



Source: Economic Survey

(III) DIRECT TAX REVENUE AS A PERCENTAGR OF GROSS DOMESTIC PRODUCT AT CURRENT MARKET PRICES

The following table 3 shows direct tax revenue as a percentage of GDP at current market prices.

YEAR	INCOME TAX	CORPORATE TAX	TOTAL DIRECT TAX
1990-91	0.09	0.09	1.09
1991-92	4.06	3.06	8.03
1995-96	1.03	1.04	2.08
2000-01	1.05	1.07	3.03
2005-06	1.05	2.07	4.03
2010-11	1.08	3.08	5.06
2012-13	1.09	3.07	5.06

Source: Economic Survey

The above table depicts that the total direct tax revenue as percentage of total GDP has shown an overall tendency to increase with fluctuation during the period. It has increase from 1.9 percent from the year 1990-91 to 5.6 percent in year 2012-13. The two major component of direct tax revenue has also shown same tendency. The income tax revenue has increased from 0.9 percent in the year 1990-91 to 1.9 percent in the year 2012-13 and for the same period corporation tax has increased from 0.9 percent to 3.7 percent.

(IV) COMPARISON OF TRENDS IN TAX GDP RATIO

(1990-91 to 2001-02,2002-03 to 2007-08 and 2007-08 to2014-15)

Comparison of trend in tax GDP ratio between 1990-91 to 2001-02,2002-03 to 2007-08 and 2007-08 to 2014-15 is shown in below table-4.

Table 4- TRENDS IN TAX GDP RATIO

NAME OF TAX	GROWTH RATE		
	PERIOD I 1990-91 TO 2001-02	PERIOD II 2002-03 TO 2007-08	PERIOD III 2007-08 TO 2014-15
INCOME TAX	18.57	21.29	17.46
CORPORATION TAX	19.58	31.80	12.13
TOTAL DIRECT TAX	19.29	27.76	14.00

Source: Budget documents, Ministry of Finance.Govt.of India

The above table depicts the growth rate of direct tax and its main component under three phases. It clearly shows that the growth rate of total direct tax increase from 19.29 percent in period I to 27.76 in period II but in period III growth rate decline to 14 percent, the reason may be global financial crises. The growth rate of Income tax decline from 18.57 percent to 17.46 percent in period II. Thegrowth rate was 21.29 percent in period III. On the other hand growth rate of corporation tax was 19.5 percent in period I it increases to 31.80 percent in period II and mark a decline in period III with only 12.13 growth rate. From above analysis it is clear that the growth of Income tax remainsstatic as compare to corporation tax and total direct tax.

CONCLUSION

The impact of the direct tax reforms on collection of tax revenue has been assessed in this study. Based on such analysis the paper concludes that there have been major changes in tax system of India due to Tax reforms in India .The receipt of direct tax has increased considerably on account of tax reform, from 10103 cr in 1991-92 to 732892 cr in 2018-19.It can be concluded that there is satisfaction in case of receipts of direct tax revenue after the tax reforms in India. Although tax -GDP ratio has declined in 1990s when the reform process was initiated, it is not that strategy of tax reforms has not worked. The decline in Tax-GDP ratio is partly due to the 'costs of reforms' reflecting reduction in taxes to increase competition and enhance efficiency.

As far as direct taxes are concerned, strategy of reforms appears to be working well.From 1.9percent of GDP in the year 1990-91 ,contribution of direct taxes increases to 5.6 percent in the year 2012-13.Share of direct taxes in the total tax revenue of the centre has gone up from 19.15 percent in 1990-91to about 52.4 percent in the year 2012-13.Thus over the years the government has been quiet successful in raising direct tax revenues. The trend is expected to continue in the future as well, it clearly indicates that the strategy of tax reforms followed since 1991 is basically working. The growth rate of direct taxes also increases during the period under study. It increases due to the various measures adopted by government for tax reforms but due to global financial crises we are failed to achieve the potential growth rate in direct taxes.

SUGGESTIONS

- Government must focus on raising the share of direct taxes as they play an important role in ensuring equality as compare to indirect taxes which are consumption based and impact everyone equally.
- To augment revenue from personal income tax the government should broaden the tax paying population. It can be done in two ways. Firstly, by bringing large numbers of potential tax payers into the Growth of Income net and secondly by eliminating the tax exemption and deduction.
- In the case of corporation taxation too there is a need to increase the number of tax paying companies. In corporation taxation it is necessary to broaden the tax base by minimizing tax concession and preferences, which pay substantial dividends without paying any corporate income tax.
- Complexity of tax law causes tax evasion so government should take initiative for efficient tax administration and simple tax laws

- Tax reforms should as a rule be undertaken to achieve long term rather than short term objectives. Short term objectives cause frequent changes in tax system due to which tax avoidance and evasion will increase.

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