



India's Tax Compliance Levels

What is the issue?

\n\n

\n

- While a miniscule population in India files IT returns, it doesn't imply that a majority of Indians are evading taxes.
- In this context, the statement by the "Union Finance Minister", which calls for enlarging the tax net to enhance tax compliance, sounds hollow.

\n

\n\n

Is tax compliance among masses really poor in India?

\n\n

\n

- **Statistics** - In FY18, just 6.84 crore entities (inclusive of - Individuals, HUFs and Businesses) filed their Income Tax Returns.
- Among these, there were 6 crore individual assesses - which is just about 4.5% of India's total population, a miniscule minority.
- **Government's view** - Finance Minister feels that there is room for collecting more taxes from people as number of people filing IT returns is still low.
- Additionally, he has stated the low "Tax-to-GDP ratio" in India to drive his point that the ratio could be improved by another 1.5% points.

\n

\n\n

\n

- **The Flaw** - The fact that only few pay direct taxes is used to assert that the culture of tax compliance is low in India and that there is large scale

evasion.

\n

- This is a flawed logic as it ignores the fact that a vast majority of Indians earn too less to be liable to taxation.

\n

- Additionally, the fact that “percentage of tax payers” is dependent on the demographic factors like “size of the working age group” is being overlooked.

\n

\n\n

What is the demographic breakdown of India’s direct tax net?

\n\n

\n

- As per the last Census (2011), only about half of India’s population fell in the working age group of 20- to 59-year olds.
- Only half of this working-age population in turn, was employed throughout the year (main workers), implying that rest did not find regular employment.

\n

- Hence, the number of people who are in the working age group and found regular employment accounts for about 33 crore individuals.

\n

- Indian tax laws offer a complete exemption to agricultural sector, which employs the largest category of India’s working population.

\n

- The 2011 census tells us that roughly half of the main workers were either cultivators or agricultural labourers.

\n

- Hence, this effectively leaves just about 16.5 crore people who can be realistically expected to pay taxes.

\n

- Of this, 6 crore are already in the IT net, despite the extremely low levels of income that the masses earn, which is in fact a good number.

\n

\n\n

Do a majority of taxable workers earn below taxable levels?

\n\n

\n

- India’s slab system exempts the first Rs. 2.5 lakh of annual income (from all

sources — salary, property, business, profession and others) from tax.

\n

- Census doesn't provide us with data regarding earning levels of workers or self-employed folk, which would've helped in devising the exact tax net.

\n

- But Labour Bureau's "Annual Employment Surveys" do provide anecdotal evidence on the income levels for a large sampling of Indian households.

\n

- The latest survey in FY16 covered 1.5 lakh households and found that over 87% of the households (across domains) earned less than Rs. 2.4 lakh a year.

\n

- This effectively means that only 13% of the 25 crore Indian households (about 3.2 crore households), may be earning enough to pay income tax.

\n

- Hence, number of tax payers is not abysmally below rationally expected levels.

\n

\n\n

How does the corporate tax landscape look?

\n\n

\n

- Corporate tax collections in India seem to be afflicted by the poor scale and low profits reported by the vast majority of businesses.

\n

- In India, business is dominated by the 6.3 crore unincorporated enterprises that are mostly run from home and registered companies are just 17 lakh.

\n

- Of the registered companies, only about 11 lakh are active and about 7 lakh companies filed their I-T returns in FY17.

\n

- But again, as many as 5.3 lakh of those companies reported an annual income of less than Rs. 2.5 lakh.

\n

- Between FY14 and FY18, India saw the number of I-T return filers expand by 80% from 3.79 crore to 6.84 crore.

\n

- But the direct tax kitty grew by a far lower 55% as nearly a fourth of the current return filers fall in the zero-tax bracket.

\n

\n\n

What could be concluded from the above?

\n\n

\n

- **Inferences** - The above calculations are rough because they are based on the data available in the public domain.

\n

- But they do suggest that low IT filings may not be the biggest cause of India's low tax mop-up, as the government seems to believe.

\n

- Going by the number of taxpayers, at 6.84 crore, the direct tax base is already at pretty healthy levels once we account for legitimate exemptions.

\n

- Tax collection is low due to poor household incomes, lack of formalisation of businesses and under-reporting by some high-profile assesses.

\n

- **Way ahead** - Policy makers need to realise that, merely identifying non-filers and scrutinising them might not enhance tax collection significantly.

\n

- The only logical way to expand tax base at present is to bring agriculture into the taxable net and also tax those earning below Rs. 2.5 lakhs.

\n

- As both of these could prove politically costly, the finance minister will have to rather focus on methods to improve income levels of the masses and firms.

\n

- Sustaining the ongoing economic revival, creating more formal sector jobs and formalising small businesses through GST-like reforms is hence the best bet.

\n

\n\n

\n\n

Source: Business Line

\n



IAS PARLIAMENT

Information is Empowering

A Shankar IAS Academy Initiative