

Personal Income Tax Structure In India: An Evaluation

Dr. Radha Gupta*

In the present paper an attempt has been made to throw light on prevailing personal income tax structure in India. The paper briefly analyses the issues relating to high tax burden on people falling under low and medium income groups. Researcher concludes that there is still a need to bring more reforms in the personal income tax structure in the form of broadening the exemption limits, lowering the tax rates, reorganizing the different income tax slabs and simplify overall tax procedure so that people could be encouraged for compliance of tax laws.

Keywords: Structure, Slabs, Reorganizing, Exemptions, Broadening.

Introduction

As per Income Tax Act 1961, every person (Individuals, Companies, Hindu undivided families, Firms, Cooperative Societies and all other artificial judicial persons) whose total income exceeds maximum exemption limit is liable to pay income tax at the rates prescribed in the act. It is not a voluntary payment but an enforced contribution that is why tax is known as financial charge or levy. Despite the fact that money provided by taxation is used to carry out many functions for the welfare of the society, it usually gives a feeling of displeasure to tax payee. Actually, tax payer does not want that his hard core earned money should be taken away from him. History is witness that there is always a struggle between tax payer and tax collector. This may be due to the irrational structure of Personal Income tax. The tax rates, tax base and tax slabs in Personal Income Tax schedule were exorbitantly higher by any standards during the period under review. The need for rationalization of tax structure was felt long back but very little reform has been seen so far.

Review of literature

It is a matter of general belief that taxes on income and wealth are of recent origin but there is enough evidence to show that taxes on income in some form or the other were levied even in primitive and ancient communities. (IT circular, 2010). India has a tax charter with three-tier federal structure (Union, state governments. & local bodies). (Bernardi, 2005) The rapid changes in administration of direct taxes, during the last decades, reflect the history of socio-economic thinking in India. (CBDT report, 2009) Governments use different kinds of taxes and vary tax rates because taxes are one of the significant sources of revenue. (Asia trade hub .com) Quite apart from its role of raising revenue, the personal income tax has long been regarded as a potent weapon of effecting distributive justice (Nayak, 1989). Secondly, it is an instrument of equity, social justice and income

distribution. (Sahota, 1961) Another common and most empirically used way to understand its role is the ratio of personal income tax to total tax revenue and national income. (Agarwal, 1991) A good tax system is characterized by a high responsiveness of tax revenue to changes in income of public bodies or national income; the technique of measuring this response is tax elasticity and tax buoyancy. Tax policy forms an important part of development process in a developing economy. The total tax revenue is dependent upon three variables viz., tax rate, tax base, and national income. (Ankita, 2009) Tax reforms sometime bring changes in taxation system. A tax payer sometime finds it difficult to understand whether change in tax liability is due to legislative change in the federal tax code or shift in his or her own circumstance. (Troy et al) There has been change in Personal income tax rates, tax brackets and rate of surcharges from time to time. As rates remained stable since 1997-98, at 10, 20, and 30%, with some changes in the associated tax brackets. A surcharge of 5 % of the income tax payable was imposed in 2002-03 in the wake of the Kargil war and was discontinued the following year. It was replaced, however, with a separate 10 % surcharge imposed on all taxpayers with taxable incomes above ₹ 850,000; the level was raised to ₹ 1million in the 2005-06 budgets. (Rao et al)

Objective of the Study The objectives of the study are

1. To measure the trend of personal income tax structure in India.
2. To determine the present scenario and future prospects of prevailing income tax structure.
3. To suggest suitable measures for rational personal income tax scheme.

Limitations and Scope of the Study

Personal income tax in India may be said to consist of taxes on

*Assistant Professor, Baba Ghulam Shah Badshah University, Rajouri. Jammu and Kashmir

the non-agricultural incomes of three types of assesses: Individuals, Hindu Undivided families, unregistered firms and other associations of persons. However, present study is confined only to general tax payers. Hence, there is further scope of study.

Research Methodology

Present study is descriptive and exploratory in nature. Here researcher has taken 12 financial years (2000-2001 to 2011-2012) personal income tax rate and calculated tax burden accordingly. Various books on direct taxes, indirect taxes, public finance, circulars of CBDT, reports in newspapers, research papers in journals and magazines, statistics based on various issues of economic survey of govt of India, various internet sites, and other relevant literature were consulted. Guidance of the experts in the field and view of public is also considered for carrying out the study.

Present study has passed through the following stages:

1. Composition and comparative analysis of income exempted from tax.
2. Composition of total tax liability of general tax payer for period under review.
3. Composition of growth rate of tax burden.
4. Composition of tax liability on different income slabs.
5. Conclusion and suggestions.

Composition and comparative analysis of income exempted from tax.

Table 1. under reference depicts tax free income of male, female and senior citizen. Study shows that exemption limit remained constant for first six financial years under review, despite raising cost of living and additional requirement for better life. Although the increased proportion of tax free income thereafter is significant but the pace has not been in consonance with raising prices all around.

Table 1.

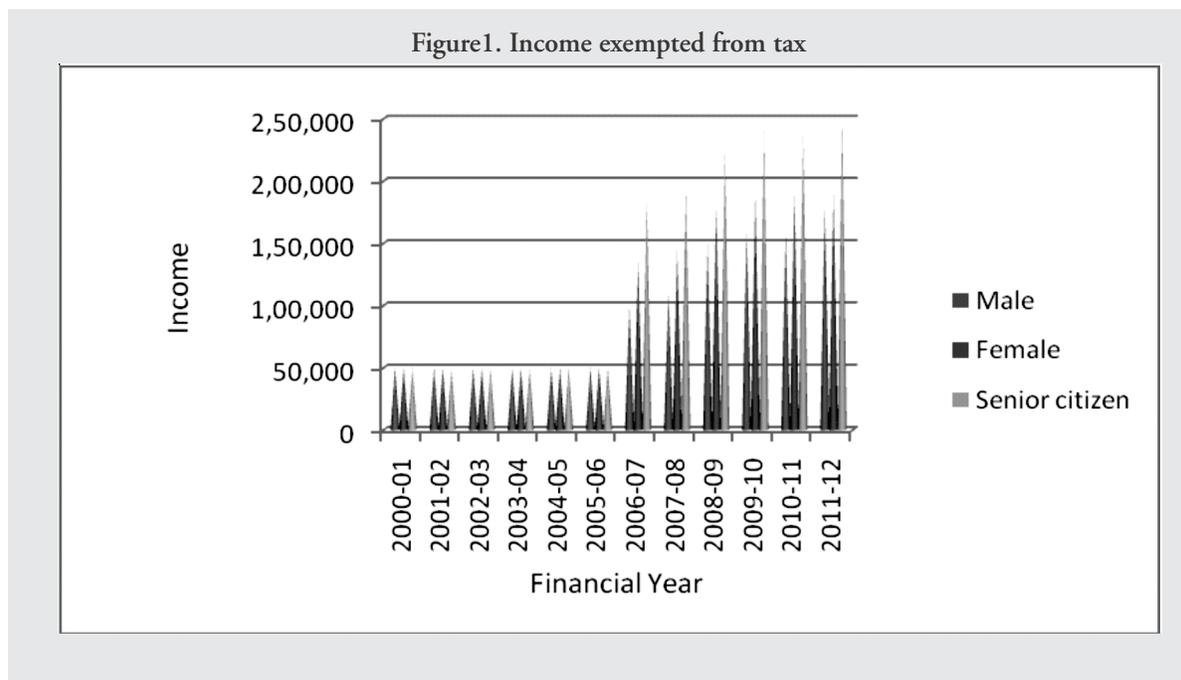
Tax Free Income for Male, Female and Senior Citizen

Financial Year	Male	Female	Senior citizen
2000-01	₹50,000	₹50,000	₹50,000
2001-02	₹50,000	₹50,000	₹50,000
2002-03	₹50,000	₹50,000	₹50,000
2003-04	₹50,000	₹50,000	₹50,000
2004-05	₹50,000	₹50,000	₹50,000
2005-06	₹50,000	₹50,000	₹50,000
2006-07	₹100,000	₹135,000	₹185,000
2007-08	₹110,000	₹145,000	₹195,000
2008-09	₹150,000	₹180,000	₹225,000
2009-10	₹160,000	₹190,000	₹240,000
2010-11	₹160,000	₹190,000	₹240,000
2011-12	₹180,000	₹190,000	₹250,000

(Source: Data compiled from budget highlights given in newspapers)

In the year 2011-12, a new category called "Very senior citizen" has been added for people above 80 years. Now we have two types of senior citizens "Senior citizen" up to 60 years of age and "Very senior citizen in the age of 80 year or above. The threshold limit of income exempted from tax for newly created

category of assesses is ₹ 500,000, thereafter they have to pay tax according to prevailing tax rates. Interesting point here is that higher the amount of income exempted from tax, lever the number of individual who will fall in the last category



2. Composition of total tax liability of general tax payer for period under review

Table 2.

Trend of Tax Rates and Tax Liability for General Tax Payers

Financial Years	Income (in ₹)	Rate	Liability (In ₹)	Income (in ₹)	Rate	Liability (in ₹)	Income (in ₹)	Rate	Liability (In ₹)
2000-01	50,001 to 60,000	10%	1000	60,001 to 150,000	20%	18,000	150,001 to 900,000	30%	135,000
2001-02	50,001 to 60,000	10%	1000	60,001 to 150,000	20%	18,000	150,001 to 900,000	30%	135,000
2002-03	50,001 to 60,000	10%	1000	60,001 to 150,000	20%	18,000	150,001 to 900,000	30%	135,000
2003-04	50,001 to 60,000	10%	1000	60,001 to 150,000	20%	18,000	150,001 to 900,000	30%	180,000
2004-05	50,001 to 60,000	10%	1000	60,001 to 150,000	20%	18,000	150,001 to 900,000	30%	180,000
2005-06	100,001 to 150,000	10%	5000	150,001 to 250,000	20%	20,000	250,001 to 900,000	30%	225,000
2006-07	100,001 to 150,000	10%	5000	150,001 to 250,000	20%	20,000	250,001 to 900,000	30%	225,000
2007-08	110,001 to 150,000	10%	4000	150,001 to 250,000	20%	20,000	250,001 to 900,000	30%	225,000
2008-09	150,001 to 300,000	10%	15,000	300,001 to 500,000	20%	40,000	500,001 to 900,000	30%	150,000
2009-10	160,001 to 300,000	10%	14,000	300,001 to 500,000	20%	40,000	500,001 to 900,000	30%	150,000
2010-11	160,001 to 500,000	10%	34,000	500,001 to 800,000	20%	60,000	800,001 to 900,000	30%	60,000
2011-12	180,001 to 500,000	10%	32,000	500,001 to 800,000	20%	60,000	800,001 to 900,000	30%	60,000

(Source: Data compiled from newspapers and direct tax reports)

Composition of total personal income tax liability (tax on all the three slabs in each financial year) of individual tax payer from FY 2000-01 to 2011-12 is shown in table 2. Here taxable income up to ₹ 900,000 is taken into consideration and tax load on each slab is calculated accordingly. Tax liability on first income bracket varies between ₹1000 to ₹ 32000 for entire period under review. In case of second income bracket, it is ₹ 18,000 in 2000-2001 and 60,000 in 2011-12. Surprisingly, in case of third income bracket, liability is maximum in the beginning (₹ 135,000) and minimum in the end (₹ 60,000). However, total tax load is showing decreasing trend but this is one side of the coin because those who fall in the third income bracket are people with high income level. Increasing trend of tax load in case of first and second income slabs during the

period under review indicates that those who fall in the low and medium income group are highly taxed than their counterparts who are in the third income bracket. Furthermore, the growth rate of total tax load, which is given in table 3, varies between 27.11% to 16.88% between 2000-01 to 2011-12. Keeping in view the growth rate of taxes on first and second income groups there is ample justification to say that there is need to bring reform in prevailing personal income tax structure in the form of lower tax rates. Due to inflationary tendency in the country, those who fall in tax bracket feel double snag, which can affect adversely their sustainability on the one hand, and willingness to contribute for tax payments on the other.

3. Composition of growth rate of tax burden from 2000-2012

Table.3

Growth Rate of Tax Liability (2000-01 to 2011-12)

Financial Years	Tax load on first slab (in ₹)	Tax load on second slab (in ₹)	Tax load on third slab	Total tax load (in ₹)	Total taxable income in (₹)	Tax liability (in %)
2000-01	1,000	18,000	225,000	2,44,000	₹9,00,000	27.11
2001-02	1,000	18,000	225,000	2,44,000	₹9,00,000	27.11
2002-03	1,000	18,000	225,000	2,44,000	₹9,00,000	27.11
2003-04	1,000	18,000	225,000	2,44,000	₹9,00,000	27.11
2004-05	1,000	18,000	225,000	2,44,000	₹9,00,000	27.11
2005-06	5,000	20,000	195,000	2,20,000	₹9,00,000	24.44
2006-07	5,000	20,000	195,000	2,20,000	₹9,00,000	24.44
2007-08	4,000	20,000	195,000	2,19,000	₹9,00,000	24.33
2008-09	15,000	40,000	150,000	2,05,000	₹9,00,000	22.77
2009-10	14,000	40,000	150,000	2,04,000	₹9,00,000	22.66
2010-11	34,000	60,000	60,000	1,54,000	₹9,00,000	17.11
2011-12	32,000	60,000	60,000	1,52,000	₹9,00,000	16.88

(Source: Data compiled from information given in table 2.)

Composition of tax liability on different slabs for the period under review

In this section, the researcher has calculated tax load on different slabs, which is shown in table 4, and their growth rates in corresponding tables. Though time to time composition of sum covered, in different tax, slabs have been

changed but by and large in our country people fall in first two slabs according to their income labels and they are known as Aam Adami. Tax burden on different slabs gives us a different picture and this is virtually a clear position because those assesses whose incomes cover all the three slabs are people with high income level and those who fall in first and second tax brackets are middle income group people.

Table. 4
Tax Weight on General Tax Payer of Different Slabs

Financial Year	Tax burden on First slab	Tax burden on Second slab	Tax burden on Third slab
2000-2005	₹1,000	₹18,000	₹225,000
2005-2007	₹5,000	₹20,000	₹195,000
2007-2008	₹4,000	₹20,000	₹195,000
2008-2009	₹15,000	₹40,000	₹150,000
2009-2010	₹14,000	₹40,000	₹150,000
2010-2011	₹34,000	₹60,000	₹60,000
2011-2012	₹32,000	₹60,000	₹60,000

Table 5.
Trend of Tax Load on First Slab

Financial Year	Growth rate (In %)
2000-2005	---
2005-2007	400
2007-2008	300
2008-2009	1400
2009-2010	1300
2010-2011	3300
2011-2012	3100

(Source: Data in Table 4)

Tax toll is quite heavy on those who fall in first tax bracket, which is portrayed in the form of corresponding high growth rate in tax burden, in table 5. Continuously higher dose of tax on low income is exposing inverse relationship between

incomes earned by assesses and degree of tax imposed on them. Proper care therefore is, needed on the part of tax administration to have low tax liability at lowest level so that people should act in accordance with tax law.

Table 6
Trend of Tax Load on Second Slab

Financial Year	Growth rate (In %)
2000-2005	---
2005-2007	11
2007-2008	11
2008-2009	122
2009-2010	122
2010-2011	233
2011-2012	233

(Source: Data in Table 4)

Situation is not much different for those who get under next tax bracket but the only difference in this case is that tax toll is increasing at slightly lesser speed than their counterparts are. Overall tax liability on lower and middle income groups is higher than high earning people in the country, which is the violation of “Equity Principle” of taxation given by Adam

Smith. An important task, therefore, before tax administration is to design the rate schedule that should be equitable and efficient otherwise people will start following unethical practice in the form of tax evasion, which could have negative impact in the growth story of the country.

Table 7.
Trend of Tax Load on Third Slab

Financial Year	Growth rate (In %)
2000-2005	---
2005-2007	-13
2007-2008	-13
2008-2009	-33
2009-2010	-33
2010-2011	-73
2011-2012	-73

(Source: Data in Table 4)

Comparatively, third tax bracket carries less tax toll than first and second slab. Table 7 under reference depicts that growth in tax burden is 33% in 2003-04 and it has been reduced thereafter up to 11%. Another way to bring reform in personal income tax structure is that number of tax slabs should be few and their range fairly large to minimize the distortion arising out of bracket creep. Findings of many researchers have shown that reduction in tax rate has caused positive impact on tax buoyancy.

Conclusion

Though the payment of tax is a moral obligation and tax payer is aware about the fact that revenue generated by government through taxes is used for the welfare of the society but due to high personal income tax rates and other irrationalities in prevailing tax constitution, assesses feel bit pinched while contributing toward this noble cause. This situation develops ill feeling toward payment of income tax which results assesses make every attempt to hide their income and avoid tax payments, which is a major setback in economic growth of a country. Need of the hour is to bring reforms in present tax regime by framing tax friendly policies so that those who come under tax trap should willingly come forward and feel pride to pay tax. In order to further bring them into make them feel comfortable Basic exemption limit must be at moderate level. The tax brackets required to be redesigned and tax tariff is needed to be reframed in such a way that high tax should be imposed on high income and lower income should be taxed with lower rates.

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