

## 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.

\n

- 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.

\n

- Among these, there were 6 crore individual assesses - which is just about 4.5% of India's total population, a miniscule minority.

\n

- **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.

\n

- 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.

\n

- 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

