Fundamental of Taxation in India

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Abstract: The main source for development of every Nation is revenue and revenue is generated by taxes, therefore the smooth taxation system is an essential need. A consistent economic growth is possible only where the system of taxation is even. In India the taxation system was acquired since ancient epoch and with change of time was consistently modified. The taxation system of modern India is being embodied in the Constitution of India and governance of taxes is channelized in accordance to the constitution.

Current work is primary based on knowing the fundamental of taxation and includes the analysis of canons of taxation which strengthens the taxation system.

Keywords: Taxation, Canons of taxation, Revenue, Tax and Constitution.

1. **Historical Background:** The concept of collection of tax in India was originated from ancient period and the evidence is found in Manu Smriti and Kautilya Arthashastra, whereby chapter seven of the Manu Smriti has many provisions for levy of taxes for instance shlok no eighty states: "Let him cause the annual revenue in his kingdom to be collected by trusty (officials), let him obey the sacred law in (his transaction with) the people and behave like a father towards all men". Similarly shlok no 128 states that" After (due) consideration the king shall always fix in his realm and duties and taxes in such a manner that both he himself and the man who does the work receives (their due) reward (Panda, 2014). Similarly the concept of taxation was provided by Kautilya in his famous writing on Arthashastra, where he has strongly recommended a linear incometax and has put emphasis on fairness and stability of tax structure, fiscal federalism, avoidance of heavy taxation, ensuring of tax compliance and subsidies to encourage capital formation etc (Sihag, 2009)

   This concept of taxation is systematically personified in medieval India and were unfortunately vicious and disparaging during the mughal period where various kinds of taxes were imposed on the individuals.for instance alauddin khilji imposed a direct Kharaj tax amounting to a maximum of 50 percent of the agricultural produce (Express Web Desk, 2018).

   Further with the arrival of Britishers the system of taxation was reformed the main cause to reform tax law was first freedom movement in 1857 it was mutiny against the british government. Aftermath of mutiny of 1857 was the passing of the Government of India Act,1858.

   In the yeaar 1860 when Sir James Wilson introduced the First Union Budget on april 1860 the tax was also introduced and it led to the enactment of Income tax Act, 1860 the act was enacted to recover the losses which occured due to mutiny. Later on in year1886 a separate Income Tax Act 1886 was passed in this Act income was divided into four schedules and taxed seprately namely (1) Salaries, pensions or gratuities (2) Net profits of companies; (3) Interests on the securities of the Government of India; (4) Other sources of income. The Act of 1886 was repealled by The Income Tax Act 1918 and in Year 1922 the new Income Tax Act was passed which replaced the Act of 1918 and even after getting independence it continued for more than a decade (Tarun, 2020).

   After independence, India has established herself as a welfare State and to fulfill the obligation of welfare revenue is needed, this revenue was collected through taxes imposed on the citizens and person who are earning income in the Indian jurisdiction. To legalize the tax imposed on income the Government of India with the consultation of ministry of law enacted the Income Tax Act, 1961 and it came into force on 1 april 1962. The Act was amended time to time as per requirement. The recent amendment was published with the passing of the Finance Act, 2020.

1.1. **Tax Meaning:** According to Black's Law Dictionary **"**Tax means A monetary charge imposed by the government on persons, entities, transactions, or property to yield public revenue. Most broadly, the term embraces all governmental impositions on the person, property, privileges, occupations, and enjoyment of the people, and includes duties, imposts, and excises. Although a tax is often thought of as being pecuniary in nature, it is not necessarily payable in money" (Garner, 2004).

According to Webster's New World Law Dictionary, tax means " A charge assessed on an individual or on property for the purpose of supporting the functioning of the government. Such charges may be imposed on sale of property or goods, imports, exports, wages and income, privileges, and just about anything else that one can think of. Although usually thought of as being monetary in nature, it is not necessarily so.” (Wild, 2006)

Thus it can be concluded from these two definitions that tax means any monetary charge which is imposed by the Government on person, entities or whomsoever specified by the government in the course of law to earn public revenue for the welfare of public.

1.2. **Need for Tax:** Taxes are mandatory as the revenue collected from same is utilized by the government for public welfare purposes. It is through the tax by which, a Nations infrastructure is developed, along with it also balances the economy through transparent flow of the funds. By depositing tax timely and regularly every tax payer not only participates in strengthening the Nation but also fulfills his duties towards Nation (Kaplow, 2006).

2. **Canon of Taxation:** By canons of taxation we simply mean the characteristics or intrinsic worth which a good tax system should possess. Adam Smith was the first person who in 1776, acknowledged the significance of the compliance costs of taxation in his four famous maxims or canons of taxation (Lamb et al., 2005) namely the principles of equity, certainty, convenience, and economy. These four principles are effectively functional in modern period, with expansion of time and upgradation in tax laws, the modern economist have also added few principles to theAdam Smiths canon of taxation namely Canon of productivity, Canon of elasticity, Canon of simplicity, Canon of diversity and Canon of Expediency (Team, 2020).

2.1. **Canon of Equality:** Canon of equality states that encumberance of tax must be disseminated uniformly or equally among the taxpayers according to the ability of taxpayers. Tax liability according to ability is the essence of canon of equality.

2.2. **Canon of Certainity:** The tax which an individual has to pay should be certain and not arbitrary. According to Adam Smith, the time of payment, the manner of payment, the quantity to be paid, i.e., tax liability, ought all to be clear and plain to the contributor and to everyone. It must be certain to the taxpayer as well as to the tax-levying authority. This principle of certainity was in direct confirmity with the principle of rule of law (Ikeda, 2012).

2.3. **Canon of Convenience:** According to Adam Smith “Every tax ought to be levied at the time, or in the manner in which it is most likely to be convenient for the contributor to pay it.” By this canon it simply laid the principle that, taxes should be levied and collected in such a manner that it provides the greatest convenience, not only to the taxpayer but also to the government. Thus, it should be painless and trouble-free as far as practicable (Kotnala, 2018).

2.4. **Canon of Economy:** According to Adam Smith “Every tax ought to be so contrived as both to take out and to keep out of the pockets of the people as little as possible, over and above what it brings into the publick treasure of the state.” (Ikeda, 2012). According to this principle, any tax that rivet high administrative cost and unusual delay in assessment with high collection of taxes should be avoided altogether (Kotnala, 2018).

2.5. **Canon of Productivity:** According to renowned economist Charles F. Bastable, taxes must be productive or cost-effective. It simply means that the revenue generated from any tax must be a fruitful one, further, this canon states that only those taxes should be imposed that do not hamper productive effort of the community.

2.6. **Canon of Elasticity:** According to this Canon the principle which modern economist want to emphasize is that the taxation system should not be rigid there shall be sufficient flexibility that the taxes should be levied in such a way that the rate of taxes can be changed according to requirement of the state of affairs. The tax system should be flexible so that taxes may be increased or decreased as per the needs of the government. Thus, income tax rates may be revised upwards or downwards as per the requirements of the government from time to time.

2.7. **Canon of simplicity:** this principle states that the taxation system shall be simple and shall not be complicated and easy to understand. If the tax system is complicated then the taxpayer will evade the tax system and on same instance it will be cost effective as there will be the requirement of tax consultant

2.8. **Canon of Diversity:** According to this principle the tax constitution shall be dynamic as it will insist the involvement of majority of sectors from diverse population and thus will also enable the state to distribute burden of taxation on every section of the society.

2.9. **Canon of Expediency:** According to this canon, a tax should be such that it requires no justification and it should not be a subject of any criticism.

Thus from the discussion it can be clearly observed that for a good taxation system these are some basic principles which shall be constantly implemented these canons are general guidelines by which the taxation system can be regulated with ease.

3. **Constitutional Validity of Taxes in India:** The Constitution of India is the supreme law of India. Any tax law, which is not in conformity with the Constitution, is called ultra vires and will be invalid. The basic of tax system was provided by the constitution of India where the powers are conferred on both the Union and State separately and jointly. Whereby Article 265 of the Constitution states that no tax shall be levied or collected except by the authority of law. It means tax proposed to be levied must be within the legislative competence of the legislature imposing the tax. Article 246 in assemblage with Schedule VII of the Constitution of India enlisted the subjected matter of tax in respective three lists namely Union list, State List and Concurrent list. In all three list namely following subject matters regarding tax are specified

3.1. **Union List:** Where only Central Government has power of legislation on subject matters covered in the list. Regarding taxes following are the entries in Union list:

- Entry No. 82:- Tax on Income other than agriculture income
- Entry No. 83:- Duties of customs including export duties.
- Entry No. 84:- Duties of excise on goods manufactured or produced in India namely petroleum crude, high speed diesel, motor spirit, natural gas, and aviation turbine fuel, tobacco and tobacco products.
- Entry No. 85:- Corporation tax
- Entry No. 86:- Taxes on capital value of the assets, exclusive of agricultural lands, of individuals and companies; taxes on the capital of companies
- Entry No.87:- Estate duty in respect of property other than agricultural land
- Entry No.88:-Duties in respect of succession to property other than agricultural land
- Entry No. 89:- Terminal taxes on goods or passengers, carried by railways, sea or air, taxes on railway fares and freight.
- Entry No. 90:- Taxes other than stamp duties on transactions in stock exchanges and future markets.
- Entry No. 91:- Rates of stamp duty in respect of bills of exchange, cheques, promissory notes, bills of lading, letters of credit, policies of insurance, transfer of shares, debentures, proxies and receipts.
- Entry No. 92 A: - Taxes on sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-state trade or commerce or
- Entry No. 92B:- Taxes on consignment of goods (whether the consignment is to the person making it or to any other person) where such consignment takes place in the course of Inter-state trade or commerce
- Entry No. 96:- Fees in respect of any matters in the Union List, but not including fees taken in any court.
- Entry No. 97: Any other matter not enumerated in List II or List III including any tax not mentioned in List II and List III.

3.2. **State List:** Where only State Government has power of legislation on subject matters covered in the list. Regarding taxes following are the entries in State list:

- Entry No. 46:- Taxes on agricultural income
- Entry No. 51:- Duties of excise on the following goods manufactured or produced in the State and countervailing duties at the same or lower rates on similar goods manufactured or produced elsewhere in India:-

- a. Alcoholic liquors for human consumption; b. Opium, Indian hemp and other narcotic drugs and narcotics, but not including medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph (b) of this entry.
- Entry No. 53:- Taxes on the consumption or sale of electricity.
- Entry No. 54:- Taxes on the sale of petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas, aviation turbine fuel and alcoholic liquor for human consumption, but not including sale in the course of inter-state trade or commerce or sale in the course of international trade or commerce or sale in the course of international trade or commerce of such goods.
- Entry No. 56:-Tax on goods and passengers carried by road or inland waterways.
- Entry No. 60:- Tax on professionals, trades, callings and employment.
- Entry 61:- Capitation taxes
- Entry 62:- Taxes on entertainments and amusements to the extent levied and collected by a Panchayats or a Municipality or Regional Council or a District Council.

3.3. **Concurrent List:** Where both Central &State Government can pass legislation on subject matters. Regarding taxes following are the entries in Concurrent list:

- Entry 43:- Recovery in a state of claims in respect of taxes and other public demands, including arrears of land revenue and sums recoverable as such arrears, arising outside that State.
- Entry 44:-Stamp duties other than duties or fees collected by means of judicial stamps, but not including rates of stamp duty.
- Entry 47:- Fees in respect of any of the matters in this List, but not including fees taken in any court.

3.4. **Constitutional Distribution of Revenues:** Indian Constitution specifies about the distribution of revenues is stated expressly under constitution and can be observed under following Articles:

- Article 268: duties levied by the union but collected and appropriated by the state
- Article 269: tax levied and collected by the union but assigned to the states
- Article 270: taxes levied and distributed between the Union and the states

4. **Classification of taxes:** Taxes are generally classified into two broader groups Direct Taxes and Indirect taxes.

4.1. **Direct Taxes:** A direct tax is alleged to be abided by the person upon whom it is assessed, and not passed on to some other person (Ghuge & Katdare, 2015). For e.g. Ad valorem, property taxes, Corporation Tax, Income Tax, Gift tax all are direct taxes. The basic characteristics of an direct tax are as follows:-

- Incidence and impact fall on the same person
- Assessee, himself bears such taxes. Thus, it pinches the taxpayer.
- Levied on income E.g. Income Tax
- Progressive in nature i.e., higher tax are levied on person earning higher income and vice versa

4.2. **Indirect Taxes:** An indirect tax is that tax which is initially paid by one individual, but the burden of which is passed over to some other individual who ultimately bears it. It is levied on the expenditure of a person. For e.g. Excise Duty, Custom Duty, Sale Tax, Value Added Tax and Goods and Service Tax are Indirect taxes. The basic characteristics of an indirect tax are as follows:-

- Incidence and impact fall on two different persons
- Tax is recovered from the Assessee, who passes such burden to another person. Thus, it does not pinch the taxpayer.
- Levied on goods and services. Thus, this type of tax leads to inflation and have wider base. E.g. Goods and Service Tax (G.S.T), Customs Duty, etc.
- Regressive in nature i.e., all persons will abide the same burden of tax on goods or service consumed by them irrespective of their ability.

5. **Conclusion:** Origin of taxation in India was from ancient epoch and can be traced in Manu Smriti and Kautilya Arthashastra. The consolidation and codification of tax laws them instigated during the British Regime. The first codified statute was also presented by the Britishers and was enacted as Income Tax Act 1886.

The basic principles for smooth functioning of taxation system were presented by the Adam Smith which is also known as canon of taxation. In modern period the canon of taxation are enhanced and were adopted in the Indian taxation system.

Taxes are vital component and are divided into two major groups namely Direct tax and Indirect tax. The main aspect of collection of taxes is the development of Nation and taxation system is dual participation machinery where by both taxpayer and government participate for strengthening and expanding the Nation's economy**.**

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