



# TRUST IN THE TAXPAYER

*Budget reinvigorates debate on whether taxes can encourage spending and growth*

SURANJALI TANDON

AS THE INDIAN economy gears up for faster growth, demand revival will take centre stage. To kick-start the so far subdued growth in private investment and urban demand, Finance Minister Nirmala Sitharaman announced relief to taxpayers with incomes below Rs 12 lakh. People in this category will not have to pay income tax. The new tax regime, already beneficial, has been rejigged to offer lower rates of tax on higher incomes. What does this shift mean for the fisc and the economy in general?

Based on tax data, the median gross total income is between Rs 5 and 5.5 lakh for individual returns filed. The taxpaying population, of course, is not representative of the overall income distribution as only 6.68 per cent of the population filed income tax returns in FY 2023-24. The exemption of incomes below Rs 12 lakh affects at least 83.52 per cent of individual income tax assesses. At the same time, people with incomes above Rs 12 lakh will benefit substantially. For example, at an annual gross income of Rs 25 lakh, the benefit of reduction could be more than a third of the current tax liability. This makes the cuts quite broad-based, and the outcome will be watched very closely.

It's difficult to accurately ascertain the num-

---

Thus, the tax break could have spinoff effects in the form of more consumption or expenditure on services, which, in turn, could create jobs. It will be interesting, however, to see if the economy is responsive. The corporate tax cut did not prop up investments in the corporate sector — even where there were immediate effects, they did not last beyond a fiscal year.

bers of the Indian middle class; consumption criteria are often used to define it. This raises two questions: Did the tax cut indeed target the section of the middle class that needed relief? Will it spur the consumption of goods? The monthly consumption expenditure of households around the median is Rs 6,334 in urban areas and Rs 3,866 in rural areas. Thus, the tax break could have spinoff effects in the form of more consumption or expenditure on services, which, in turn, could create jobs. It will be interesting, however, to see if the economy is responsive. The corporate tax cut did not prop up investments in the corporate sector — even where there were immediate effects, they did not last beyond a fiscal year. In terms of the fiscal impact, the cost of the tax cut has been estimated at Rs 1 lakh crore. If the cut works to raise demand, it can augment the future flow of revenue. However, income and consumption distributions will have a role in determining if this so-called “multiplier” effect will manifest. Perhaps a more serious look at indirect taxes may provide a better path to ensuring higher consumption than income taxes.

Beyond personal income taxes, the government remains steadfast in its resolve to ease

the operation of large corporations in India, including dispute prevention and resolution measures. An oft-contested issue in direct taxes is transfer pricing — the laborious exercise of ascertaining that transactions between two related entities are priced as if they were unrelated. This takes up the administration and taxpayer's time. Often, the same issue comes up over different years. The proposal to introduce a block audit that locks in such assessment for two years means ease of compliance. Further, the rationalising of TDS thresholds and calculation of long-term and short-capital gains signals a commitment to improve compliance.

The much-awaited reform of the Income Tax Act is likely to be unveiled soon. The budget could be a precursor to reposing trust in the taxpayer. It remains to be seen what changes will be introduced. The Finance Minister suggested that the new Act would be half its present size and do away with penal provisions. Along with a more concise Act, the tax cuts announced in the budget could reinvigorate the debate on whether taxes can be instrumental in encouraging spending and growth.

*The writer is associate professor, NIPFP*