CHAPTER FOUR

TAX REFORM RECOMMENDATIONS OF DR.RAJA J.CHELLIAH COMMITTEE

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4.1 INTRODUCTION:

The Government of India constituted a committee of experts to examine the structure of direct and indirect taxes through its Resolution dated 29th August 1991 under the chairmanship of Dr.Raja J.Chelliah, former member of the Planning Commission and Finance Commission and currently, Professor-Emeritus, National Institute of Public Finance and Policy. This particular tax reform committee was appointed in pursuance of the government's commitment reiterated by the Union Finance Minister, Dr.Man Mohan Singh, in his Budget speech while presenting the Union Budget for the year 1991-92 to make the tax system simple, credible yet progressive.

The terms-of-reference of the committee were to examine and to make recommendations on -

1. ways of improving the elasticity of tax revenues, both direct and indirect, and increasing the share of the direct taxes as a proportion of the total tax revenue and of the GDP;
2. making the tax system fairer and broad-based with necessary rate adjustments, particularly with regard to the commodity taxation and personal taxation;

3. rationalization of the system of direct taxes with a view to removing anomalies, improving equity and sustaining economic incentives;
4. identifying new areas for taxation;
5. ways of improving compliance of direct taxes and strengthening enforcement.

The approach of the committee was to deliberate on the need for reforms in all important areas in the direct and indirect tax systems, in order to set the trend for inaugurating a new era in the development of tax policy, structure and administration. The committee has recommended certain radical changes to reorient the tax system in a new direction.

4.2 GUIDING PRINCIPLES OF TAX REFORMS:

The tax structure and the actual operation of the tax system would make it clear that the rational restructuring of the major taxes, improving tax administration and drastically reducing tax evasion through a combination of inducing voluntary compliance and increasing the chances of detection and punishment is a daunting task. However, it is essential that for the wellbeing of the nation, for economic progress and for ensuring an equitable sharing of the burden of taxation, this task must be taker up and accomplished. The government's grave concern in this regard is evident from the comprehensive terms-of-reference given to the committee, requiring the committee to recommend the lines of radically transforming

the system. The task before the committee, thus, was formidable because not only is the present tax structure complicated and its indirect tax component far from rational but also the tax compliance is low and tax evasion widespread. This is attrributable partly to high rates, partly to the venality of many taxpayers and partly to inefficient tax administration with its corrupt elements whose morale has also been affected by political interference.

The committee, therefore, set before itself the following guiding principles:

1. The tax system and its burden must be acceptable to the citizens, i.e. the potential taxpayers;
2. Given the past experience and the present totality of the circumstances affecting the tax system and its operation, it is better to have moderate rates with broader bases;
3. While the tax structure should be progressive, it should not be such as to induce the generation of unaccounted income and wealth;
4. The tax system must be rational from the economic point of view. For this purpose, the structure once established must remain stable unless and until the economic conditions undergo a radical transformation. Ad hoc changes from year to year will undermine rationality and reintroduce complications;
5. The tax system and the law should be as simple as possible, it should have the strictly limited objective

of raising revenues for the government in a fair and efficient manner, achieving redistribution and discouraging some industries and the use or consumption of some products as well as granting a reasonable degree of protection to the domestic industries. A simple system will have only a limited number of rates and exemptions or deduction and give the least possible discretionary power to the tax officials for interpreting the law.

6. Methods of tax administration should be moderate and tax enforcement should be visibly improved.
7. The tax reforms should be fully, or at least nearly, revenue neutral in their totality. The system should become more income elastic.

These are the guiding principles which the committee followed in formulating its tax reform proposals. There would be no point in undertaking a reform of the tax system unless the government intends to preserve the reformed structure. For this to be possible, the growth in the government expenditure must be in consonance with the growth in the government revenues, arising from the growth in the national income at more or less stable prices and the inherent elasticity of the tax system. If the growth in the expenditure is not contained within this limit, continuous increase in tax rates and alterations in tax bases become necessary. Then the reform of the system gets nullified and would soon get back to a complicated and irrational tax structure.

The ratio of tax revenues (of the centre and the states) to GDP has reached around 21.5%; as such, the government should rely on the interaction of the growth of the economy and an income-elastic tax system for obtaining increases in revenues. The traditional concept of ARM (Additional Resources Mobilzation) through annual increases in rates, alterations in basic and new levies, should be given up as a regular component of fiscal planning. Instead of accelerating growth through ARM, in the event, the cumulative effect of continuous ARM has distorted the growth pattern and has shifted the disclosure of taxable output and income. If ARM is to be avoided, on the one hand, government expenditure growth must be controlled and on the other, the tax system must be made income-elastic. It was committee's endeavour to ensure that it recommendations for reform should significantly enhance the income-elasticity of the tax system of the centre.

The committee had also referred to the importance of the acceptability of the tax system and its burden and indicated that such acceptability depended partly on the perception of the public as to how usefully and productively the government and its administration was using the proceeds of the taxes. Today in India, while the crucial role of the government is recognized in all the quarters, there is widespread feeling among the electorate that there is considerable waste in government expenditure, that there is excess staff and that the tail to teeth ratio is unduly high. And

with it all, it is gererally felt that the public which pays the taxes gets poor service and members of the public are treated often not as the masters who pay but as supplicants. The control of the growth of public expenditure, increase in its productivity and efficiency and prevention of waste with the tax laws and for generating the needed moral sanction to enforce the laws rigorously where such compliance is not forthcoming.

Thus, the control of the growth of public expenditure and a perceptible increase in its efficiency are prerequisites for the success of the tax reform programmes. It can be expected that the reformed tax system, if implemented with a reasonable degree of efficiency, would exhibit an income-elasticity between 1.1 and 1.2 percent, i.e. if the national income or the the GDP grows at 10 percent, tax revenues could be expected to grow between 11 to 12 percent. A 5.6 pecent real growth revenue growth of 6.2 to 6.7 percent. That suggests the limits to the growth of government's revenue expenditure in real terms.

The multiplication of rates flowing from reductions and end-use exemptions effectively increases categories of classification, which, in turn, increases the extent of administrative discretion as also creates administrative complications. If the reformed tax structure is to survive, the power to alter statutory rates through notifications must be drastically curtailed.

The tax system, as a whole, has to meet the resource mobilization for which the tax base has to be wide. The committee had, for that purpose, made three major recommendations:

1. Presumptive tax scheme,
2. Taxation of Capital gains,
3. Taxation of agricultural income.

4.3 PRESUMPTIVE TAX SCHEME:

Implementation of the income-tax encounters problems everywhere in the case of certain sections of the population such as farmers, self-employed persons, professionals and small enterprises, who usually do not maintain accounts in a verifiable form. In India, nearly 40 percent of the industrial output is accounted for by small enterprises. Enterprises operating in the service sector are mostly unincorporated and the bulk of them under the 'small' category. Bringing all these enterprises under taxation is beyond the capacity of any tax administration. Exemptions and concessions are also extended to the 'small' sector to encourage handicrafts, promote employment, conserve power and serve a variety of social and economic objectives.

In the case of income-tax, widening of the tax base in terms of coverage cannot proceed far unless all those who belong to the 'small' or 'medium' category and enjoy incomes which are, in reality, well above the prescribed

threshold come within the tax-fold. This is required for revenue and for raising the contribution of direct taxes to the exchequer as well as for equity. How to bring the small enterprises effectively under taxation without giving rise to excessive administrative and compliance burden is a challenging task that needs to be addressed, if the tax system is to be reformed to improve the share of direct taxes in government revenue and achieve greater equity.

Faced with the problem of determining 'actual income', many countries practising income taxation found it expedient to apply what is called the 'Presumptive Method', whereby the tax is levied on income determined or estimated on the basis of certain indicators. Presumptive taxation envisages the application of simple method for assessing the tax base. Under this method, only the income which a taxpayer could be reasonably presumed to earn in a given situation as reflected by his investment or assets or scale of business is sought to be taxed. Apart from its administrative ease, the presumptive approach is commended by fiscal experts also on equity and efficiency grounds. Presumptive taxation helps to achieve greater equity. It has also the merit of promoting efficient use of resources, as under this method, only presumed, and not actual, incomes are taxed. In practice however, income-tax assessment for large numbers of taxpayer in both industrial and developing countries is still largely presumptive.

A well-known example of presumptive taxation is the 'forfait' system of France. Under this system, the tax base is estimated by using indicators rather than accounting records. Income-tax payable by farmers, unincorporated enterprises and professionals whose gross receipts fall below the stipulated levels are assessed under the 'forfait' system. This system has the disadvantage that the tax is negotiated on a case-by-case basis. The other widely known example of presumptive taxation is the 'takshivs' of Israel, whereby certain objective indicators like physical inputs and number of employees are relied upon to estimate the income of business enterprises who do not maintain proper accounts or records. Land taxes of many countries, including the land revenue system which has been in vogue in India for centuries, essentially incorporates the presumptive principle. The Francophone Countries of West Africa rely on presumptive taxes. Such presumptive tax on gross receipts is levied on corporate entities instead of tax on net profits, thereby avoiding the problems of determining net profits. However, this kind of tax is also used elsewhere. In the early 1980s, Turkey's tax authorities noted that 85 percent of the taxpayers filing income declarations claimed to be in the lowest tax bracket; audits of cases of suspected evasion that approximately 50 percent of income was undeclared. The government introduced a system of presumptive taxation in 1983. Indicators of living standards are used to assess taxpayers filing regular tax declarations. A presumptive assessment of certain minimum tax

amounts of income are presumed to be associated with, for instance, ownership of residential property (both owner-occupied and rental), automobiles, boats, airplanes and race-horses, foreign travel and employment of personal servants. Tax is levied on the income determined by a presumptive assessment or the taxpayer's declaration whichever is greater. This system increased tax collections; 84 percent of those who filed declarations in 1985 had their tax liability based on the presumptive assessment.

Presumptive methods can also be applied to taxes on goods and services or on wealth, where valuation is difficult. However, experience in countries as different as Columbia and Korea suggests that a considerable administrative effort is still required for any type of presumptive tax to ensure, it is based on realistic criteria and applied fairly.

Examples of application of the presumptive approach can be found in the Indian income-tax too. For a long time, income from house property was assessed in the Indian Income-tax on a presumptive basis. Since 1976, the presumed income serves as the floor for assessment of house property income. This resulted from the stipulation that where the amount received or receivable by the owner is higher than the presumed rent, 'actual' will be taken into account for purposes of income taxation. Sections 44B, 44BB, 44BBA and 44BBB

of the Income-tax Act also follow the principle in as much as they prescribe percentages to be applied to gross receipts of certain businesses for computing taxable profits.

Though a modest beginning has already been made in the Budget-1992, with the introduction of the presumptive tax in respect of shopkeepers and other retail traders with an annual turnover of below Rs.Five lakhs, it needs to be further broadened to bring dependent professionals like chartered accountants and independent contractors consisting of builders, carpenters, electricians and painters into the tax net, who are likely to earn more than the taxable limits. It has now become inevitable to deviate from the normative concept of taxing incomes to presumptive tax system to attract new taxpayers into the tax net. However, the success of the presumptive tax system ultimately depends on the efficiency of tax administration. To complement the working of the presumptive tax system, other measures like legal prescription of compulsory maintenance of books of account, effective tax information system, creation of a separate research wing of experienced professionals from public finance and other related fields to evolve and suggest proper guidelines from time to time and provision of adequate deterence in the system for ensuring faithful compliance would be very essential.

The government has accepted the proposal of the presumptive tax schemes with some modifications, but has not accepted 'Estimated Income Scheme', which in the opinion of

the committee "is an important segment of our entire set of recommendations". Problems in tax assessment and scope for harassment of small assessees arise in respect of the assessment of income from businesses of smaller assessees. whose total turnover is less than Rs.20-25 lakhs. The Income-tax assessment of all assessees having income not exceeding Rs.2.0 lakhs is done by the Income-tax Officers. Much of the harassment takes place at the hands of these officers in respect of the assessees with income below Rs.2.0 lakhs. Nearly 77% of the additional demand raised by the Department is quashed on Appeal but the assessees have to spend time and money to get the over-assessment cancelled. The main reason why the committee had recommended estimated income scheme was that the majority of the income taxpayers who derive income from business of various kinds would still have to endure harassment if the normal procedure of assessment is applied to them.

4.4 CAPITAL GAINS:

The committee for the first time has informed for rationalizing the computation of income from capital-gains. The inflation impact was ignored in the earlier efforts of rationalization and in its effect, the recommendations of the committee are highly appreciated. Inflation also creates problems in income-taxation. Mainly these are:

1. Bracket Creep:

Inflation magnifies the problem of making a progressive income-tax operate in an equitable manner. With inflation, the exemption levels and the bracket limits have to be suitably adjusted upward. Since this is not often done or not done promptly or adequately, taxpayers are pushed into higher tax brackets with the rise in their nominal incomes. only with no increase or even with a fall in real incomes. Bracket adjustments for inflation is, therefore, necessary with a progressive rate schedule, with a flat rate tax, only the exemption level needs to be indexed.

2. Valuation of Income from Capital Assets:

There is an even more difficult problem, that of measuring correctly capital income under conditions of inflation. If the value of the capital invested such as bank deposits or bonds depreciates in real terms because of inflation, the interest or return earned must be reduced to the extent of capital depreciation, before applying the indexed rate schedule. But this is not usually done, so that a taxpayer who has a bank deposit of Rs.10,000/- and receives an interest payment of Rs.1,000 at 10 percent has to pay tax on the Rs.1,000 even if the inflation during the relevant year has been 10 percent and the value of his bank deposit has depreciatted by 10 percent. If the depreciation in the value of this capital asset is to be taken into account for tax purposes, then real appreciation in other capital assets

owned by the assessee, if any, should also be taken into account. It is difficult to do such adjustments for changes in the values of all capital assets owned because that would involve estimation of accrued but unrealized real capital gains and losses. The assessees who are borrowers may gain through the fall in the real interest rate under inflation. With inflation, granting normal depreciation on the basis of historic or original cost becomes inadequate. Since there are several problems with current cost accounting, for partially taking into account the impact of inflation on the cost of replacement of productive assets such as machinery, often accelerated depreciation is granted, but the rates of acceleration have to be arbitrarily set. Thus, all in all, inflation makes the income-tax fall unequally on and discriminate among incomes from capital of individuals with different portfolios and capital income from different sources as different types of economic activity. Such discrimination will mostly be unintended and inequitable. There is, no doubt, that taxpayers whose capital income comes mostly from non-appreciating capital assets (e.g. bank deposits, units of the Unit Trust of India) are treated most unfairly by income-tax under conditions of inflation and also that investment in such assets is discouraged.

3. <u>Capital Gains and "Bunching"</u>:

Finally, inflation further complicates the problem of adequate and equitable treatment of long-term capital gains.

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As pointed out earlier, with taxation of gains on realization basis, one needs to recognize the "bunching" of gains. Because of inflation, the bunched gains have to be deflated, i.e. gains have to be indexed. This means the purchase price of every sale on which long-term gain or loss is made, must be converted to the price in the year it is sold. Thus, the date of purchase must be recorded in every case and must be available for verification. Apart from such inconvenient procedure, it is not clear if the capital gains should be fully indexed while other types of incomes are not. Some simple method of ameliorating the impact of inflation and of bunching is resorted to, such as taking only half the gains into account or fixing a flat rate for long term gains. It may be noted that under a flat rate income-tax, bunching would not create a problem in most cases once the exemption level is indexed.

Since in periods of inflation, capital gains can largely be nominal, an equitable capital gains tax must provide for indexation for inflation. Indexation for inflation should ideally relate to the entire period beginning from the date of acquisition of the asset to the date of sale. However, that can give rise to considerable problems of compliance and administration. Non-availability of records of the purchase dates of assets would lead to an avoidable increase in the cost of compliance of taxpayers and the cost of verification by tax authorities. Hence, the committee recommended that:

(i) The cost of all assets acquired prior to a cut-off date be converted into the value of asset on the cut-off date;

(ii) The value of the asset should thereafter be indexed for inflation for the subsequent period of holding.

Since valuation as on 31.3.1974 has to be established for the computation of capital gains according to the present law, there would be no additional administration and compliance cost as a result of this measure. For the present, the same date may continue to be the cut-off date.

For computing capital gains for taxation, the cost of acquisition of an asset should be increased by a cost of inflation index (CII), which should be equal to 75 percent of the consumer price index for urban non-manual employees for the entire period of holding or from a specified cut-off date, as may be appropriate. Similarly, the cost of any improvement undertaken to the asset should also be inflation-indexed using the CII. The logic of limiting indexation to 75 percent of the CII is that the tax schedule applicable to other incomes will not be automatically indexed to inflation.

Inflation-indexation of the cost of the asset would require that the index should be readily available to the taxpayers. The CII is usually available only four to five months after the close of the financial year. This would be too close to the due date for filing income tax returns. The committee recommends that an asset sold at any time

during the year should be deemed to have been sold on the first day of the financial year (Refer Table 4.1 below).

Table 4.1

Cost Inflation Index for computing long-term capital gains
(Year of transfer of asset: 1992-93)

Year of acquisition of asset	CII
Prior to 1.4.1974	2.80
1974-75	2.40
1975-76	2.35
1976-77	2.35
1977-78	2.24
1978-79	2.18
1979-80	2.06
1980-81	1.89
1981-82	1.74
1982-83	1.64
1983-84	1.53
1984-85	1.43
1985-86	1.38
1986-87	1.29
1987-88	1.21
1988-89	1.14
1989-90	1.08
1990-91	1.00

Note: The cost inflation index (CII) for the assets transferred in 1992-93 will be 'A'+'B', where A=CII and B[CPI(1992-92)-CPI(1990-91)]/CPI(1990-91) for asset transferred in 1991-92.

For purposes of computation of capital gains arising on the transfer of a capital asset -

(i) A long-term capital asset be defined to mean a capital asset transferred after one year from the end of the

financial year in which the asset is acquired. To compute long-term capital gains, all long term capital assets should be deemed to have been acquired on the last day of the financial year in question and transferred on the first day of the financial year in which the transfer takes place.

(ii) The cost of all assets acquired prior to a cut-off date be converted into the value of the asset on the cut-off date. For the present, the existing cut-off date of 1.4.1974 should continue.

(iii) In case of non-corporate taxpayers, long-term capital gains duly indexed will be subject to tax at the marginal rate applicable to the assessee in the concerned year, subject to a maximum of 27.5 percent. If income other than capital gains is below the general exemption limit, the tax on long-term capital gains will be applied to the excess of the sum of other income and long-term capital gains over the exemption level. In the case of corporate assessee, the indexed long-term capital gains will be subject to a flat rate of 40 percent. When the rate of tax on corporate profits is reduced to 40 percent as per our recommendations, the rate of tax on long-term capital gains for the corporate assessees should be fixed at 30 percent.

In the case of firms, the income from capital gains should be apportioned among the partners in the ratio of

their share in the partnership. This income should be treated as capital gains in the hands of the partners.

4.5 TAXATION OF AGRICULTURAL INCOME:

The view of the Chelliah Committee is that while agriculturists whose income consists of only agricultural income or agricultural income say below Rs 25,000 per annum and non-agricultural income below the income-tax exemption limit may not be brought within the income-tax net. The agricultural income in excess of say Rs.25,000 accruing to the non-agriculturists should be brought under the tax-net to provide equity and reduce scope for tax evasion. The committee recommended that in case of individuals or any other entities having income from non-agricultural sources above the exemption level and also the income from the agricultural sources above Rs.25,000, agricultural income in excess of Rs.2,25,000 accruing to the concerned entity should be aggregated with the non-agricultural income and the tax should be levied on the total of such aggregated income.

The central government should obtain the cooperation and consent of the state governments for enacting a provision which would enable it to bring under the purview of the central income-tax agricultural incomes in excess of Rs.25,000/-

The following observations published in 'Financial Express' on 12.2.1993 provide a clue to the trend in thinking

in this regard.

"The question of directly taxing the farm incomes has begun to atttract interest and attention after a lapse of two decades. It was in the late 'sixties that official planners ran a campaign for an integrated direct tax system for all incomes. The K.N.Raj Committee, which was appointed in response to this campaign, recommended a progressive land-holding tax as more appropriate and feasible. But with populist fiscal policies gaining ascendancy, all these propositions lost their relevance and appeal.

"It is the Chelliah Committee on Tax Reforms which has revived the idea and recommended a mild form of direct tax on farm income, primarily as a way to plug income-tax evasion on the part of those who derive incomes from their urban businesses and professions as well as landed property. It has proposed that the combined income of all individuals and entities derived from both agricultural and non-agricultural sources above an exemption limit be brought within the income-tax net. An attempt in this direction was once before also made late in the 'sixties, but was promptly scotched."

Fiscal policy generally and tax measures in particular cannot be divorced from the content and direction of the overall socio-economic development process. The question

of taxing farm incomes has been raised with varying degrees of interest and emphasis since mid-'sixties. A fairly firm consensus too was arrived at one time on the desirability of levying some form of progressive direct tax system in the case of all incomes - agricultural and non-agricultural. Meanwhile, the desirability of levying some form of progressive taxes on income and wealth in general has tended to be questioned and in response to this sentiment, the central government has been reducing income and wealth-tax liability in the case of even urban incomes and wealth. For the present government to turn around in these circumstances to revive the idea of directly taxing farm incomes even in a mild form and of limited scope does not appear to be a bright idea, especially when it has also proposed that direct taxes on urban incomes, in particular incomes generated in the urban corporate sector should be progressively reduced.

The question of tax concessions to stimulate investment would appear to be as relevant in the case of urban corporate sector as the agricultural sector. If it is considered fit and proper to exempt export incomes to boost exports, it can also be argued thatn agricultural growth being equally important, agricultural incomes too should stand exempted from any form of direct taxation. The need really is for an integrated direct tax system of all incomes above a minimum level and on a progressive scale, both for reasons of equity as well as resources mobilization for investment under a

right order of socio-economic priorities.

The exclusion of tax on agricultural income is rot appreciated by fiscal experts as the elasticity of tax revenues becomes weaker thereby. Dr.Omprakash Kajipet observes in 'The Chartered Accountant' (May 1993) as under:

To broaden the tax base, agricultural income and wealth has to be brought into the tax net atleast now on a selective basis. There seems to be general agreement and a consensus among the leading economists and even among the agriculturists on introduction of tax on agricultural incomes. According to Dr.Kaushik Basu, an economist, "whether a person pays tax or not should depend on how rich he is and no the source of his richness". According to Mr.Pranab Mukherjee, the former Deputy Chairman of the Planning Commission, and presently the Commerce Minister, Government of India, while the agricultural sector has made impressive advances and the country was able to attain self-sufficiency in food grains production, the revenue collection has dropped to Rs.2 per Rs.100. These observations give a feeling that the agricultural income and wealth need to be brought into the tax-fold in an attempt to widen the tax base.

Tables 4.2 and 4.3 (on the following pages) present the data relating to the contribution of the agricultural sector to the Gross Domestic Product and the Total Tax Reverue of both central and state governments during the past ten years.

Table 4.2

Share of agricultural sector in Gross Domestic Product (GDP) - At current prices

Year	GDP at factor cost (Rs.crores)		
	Agricultural sector	Total	%-age share in Total
1950-51	5009	8979	55.8
1960-61	6990	15254	45.8
1970-71	17937	39708	45.2
1980-81	46649	122427	38.1
1981-82	52685	143216	36.8
1982-83	56151	159395	35.2
1983-84	67498	186723	36.1
1984-85	71950	20[illegible]533	34.5
1985-86	77224	233799	33.0
1986-87	82413	260030	31.7
1987-88	92379	294765	31.3
1988-89	113998	350899	32.5
1989-90	127201	401569	31.7
1990-91	153119	472599	32.4

Source: Basic Statistics relating to the Indian Economy, Centre for Monitoring Indian Economy, Vol.1, August 1992.

The aforesaid facts clearly suggest that immediate steps are needed to reverse this phenomenon of resources. Therefore, a time has now come not to ignore the agriculture any more. It needs to contribute more to the revenue of the government.

At this juncture, it would be appropriate to recall some of the Wanchoo Committee's remarks on the taxation of agricultural income.

There is urgent need for agricultural income being

Table 4.3

Taxation of Agriculture

(Rs.in crores)

Year	Taxes on agriculture			Total tax revenue of central & state governments	Col.3 as %-age of col.4
	Land revenue	Agriculture income-tax	Total		
	(1)	(2)	(3)	(4)	(5)
1951-52	48	4	52	741	7.0
1961-62	95	9	104	1543	6.7
1971-72	101	13	114	5575	2.0
1981-82	205	38	243	24169	1.0
1982-83	189	30	219	27242	0.8
1983-84	213	44	257	31525	0.8
1984-85	282	84	366	35814	1.0
1985-86	353	127	480	43266	1.1
1986-87	382	104	486	49540	1.0
1987-88	447	63	510	56976	0.9
1988-89	594	64	658	66872	1.0
1989-90	657	93	750	77257	1.0
1990-91	586	176	762	89177	0.9
1991-92	766	204	970	103137	0.9

Source: Same as Table 4.2.

subjected to a uniform tax, more or less, on par with the tax on other incomes so as to eliminate the scope for evasion of direct taxes imposed by the Union Government. ... ...

"In fact, tax burden on the urban income is relatively so high that a taxpayer having urban income of Rs.10.0 lakhs is left, after paying income tax, with almost as much income as another person having an agricultutral income of Rs.1.0 lakhs. There is no justifiable reason for this vast disparity between the tax burden on the two sectors, particularly when as a result of the Green Revolution and the price-support policy of the government, income from agrcultural holdings have been progressively rising in recent years. In the wake of Planning, the urban taxpayers have been subsidizing agricultural income by bearing the full burden of the agricultural development schemes and also sustaining high prices of foodgrains, raw materials and other agricultural produce. Consequently, there has been a one-sided flow of resources from the urban economy to agriculture. In view of the larger objective of achieving a self-sustaining economic growth, there is a pressing need for larger and larger resources and this is another good reason why agriculture should also contribute to the national exchequer in much the same way as other sectors are doing.

"

"The present system of land revenue or tax on agricultural income is neither uniform nor rational. Besides, the benefits of the Green Revolution have intensified inequalities of income and wealth in the rural sector.

"The committee considers that uniform and progressive taxation of agricultural income is urgently necessary for the purpose of ensuring that agricultural income ceases to offer any scope for tax evasion and also on grounds of equity and distributive justice."

Towards the end of taxation of agricultural income, the Chelliah Committee has suggested that the Government may choose any of the following courses as it deems feasible.

1. The Constitution may be amended by deleting the words "other than agricultural income" appearing in Entry 82 of the Union List. Entry 46 of the State List which empowers the State Governments to legislate on matters concerning "taxes on agricultural income" may also be deleted. Such a Constitutional amendment will unambiguously empower the Union Government to imposes taxes on the agricultural income.
2. The Union Government may impose income-tax on the agricultural income, provided the State Legislatures empower the union government in this behalf by necessary resolution in accordance with provision of Article 252 of the Constitution. It would be pertinent to mention

here that the estate duty has been extended to agricultural lands in certain states by resorting to this procedure.

3. Article 269 of the Constitution may be amended to include taxes on agricultural income in the list of the taxes levied and collected by the Union and the taxes so collected may be assigned to the States in accordance with the procedure outlined therein. The advantage of this course of action is that the state governments are more likely to concede the powers to impose tax as their financial interests will be statutorily protected.

4.6 DIRECT TAX CODE:

Over the issue of the Direct Tax Code, the Chelliah Committee had postponed its recommendations by stating that, "the objectives sought to be achieved by a single direct tax code are uniformity and simplicity with regard to the legislation concerning direct taxes, which is desirable. However, the Committee is of the view that before enacting the direct tax code, the government shoulld first consider the committee's recommendations and take a final view in that regard so that the code is not required to be amenced after its enactment". The committee also recommended that the entire matter of introduction of a direct tax code should be postponed till such time as the law, after implementation

of the committee's recommendations has stabilized. Further, before undertaking codification, the arrangement of sections in the code and the language used therein should be referred to a committee of experts to ensure that unintended changes in the provisions do not occur.

The draft Code should be given wide publicity so that public debate and informed comments or opinions arising therefrom could be taken into account before finalizing the Code. The Chelliah Committee's hesitation thus reflects on the haphazard effect the reform attempts so far have had on the country taxation legislation, particularly the direct tax legislations.

4.7 THE RATE SCHEDULE:

Lastly, the Chelliah Committee has also devoted its attention to the tax structure. The fairest, the simplest and the most administrable form of income-tax is a moderately progressive, flat or single marginal rate income-tax levied on a comprehensive base with a system of personal income-tax with more than one rate. The committee, therefore, has recommended the following rate schedule for different taxable entities:

1. In case of individuals, the exemption limit should be fixed at Rs.28,000. The marginal rates of tax (inclusive of surcharge, if any) should be:

a. 20% for total income in the range of Rs.28,000-50,000;

b. 27.5% for total income in the range of Rs.50,000-2,00,000;

c. 40% for total income exceeding Rs.2,00,000.

2. In case of a Hindu undivided family, the existing distinction between a specified HUF and a non-specified HUF should continue. The rate schedule for non-specified HUF should be the same as recommended in the case of the individuals; in the case of specified HUFs, the exemption limit should continue to be fixed at Rs.12,000. The marginal rates of tax (inclusive of surcharge, if any) should be 27.5% for the total income in the range of Rs.12,000 to Rs.1,00,000 and 40% for the total income exceeding Rs.1,00,000/-;

3. In case of local authorities, the tax should be levied at a proportional rate of 30%;

4. In case of domestic companies, the tax rates (inclusive of surcharge, if any) should, within the next three years, i.e. by the assessment-year 1995-96, be reduced to the same level as the maximum marginal rate of tax (inclusive of surcharge, if any) in the case of individuals, i.e. 40%. Further, the existing distinction between the companies in which the public are substantially interested and the companies in which the public are not substantially interested for the puurpose of tax rate, should also be abolished within next three years.

4.8 OBSERVATIONS:

The Raja Chelliah Committee is the latest Committee to submit its proposals on tax reform. A detailed discussion has already been offered on the scope and direction of the reforms suggested by this Committee.

The word 'reform', according to the Oxford Dictionary implies "improvement by removing faults". The Webster's Third New International Dictionary assigns the following meanings to the term 'reform': (i) to restore or renew; (ii) to amend or improve by change of form or by removal of faults or abuses; (iii) amendment of what is defective, vicious or corrupt.

Viewed from this, the tax reforms suggested by Dr.Raja J.Chelliah appear to miss the interpretation of the term 'reform'. Particularly, the following aspects have not been considered by the Committee:

(1) The entire direct tax legislation suffers from defective draftsmanship; the language used is not understandable for common taxpayer. This results into tax litigations and the taxpayers as well as the revenue authorities have to confront each other in the Court of Law.

(2) The earlier Committees on tax reforms had recommended the creation of a single direct tax code. The Chelliah Committee, though has considered the issue, has postponed any further discussion on this issue.

(3) The Chelliah Committee's report does not contain anything

specific to improve the administration of the department. In fact, there is need to improve the administration and make it more responsive to the needs of the taxpayers.

(4) The Committee has not made any recommendations relating to the taxation of agricultural wealth and capital gains on the transfer of agricultural assets, which taxes can be imposed by the central government as there is neither any Constitutional bar for this nor is the consent of state governments called for. It was expected that a Committee would be required to find ways and means for improving the tax elasticity and wedded to the concept of equity would certainly make strong recommendations to tap this source.

REFERENCES:

The above discussion is based on the following authoritative publications:

1. 'Tax Reform Recommendations', Dr.Raja J.Chelliah Committee.
2. 'World Bank Report - 1988'
3. 'The Chartered Accountant', May 1992.
4. 'The Economic Times', 2nd and 4th Sept., 1992.

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