CHAPTER-6
FINDINGS AND POLICY IMPLICATIONS

Indian economy was an economically stagnant economy at the time of independence. The framers of the Indian Constitution tried to erect a strong united India, to guarantee the cohesiveness of a vast country and to build a sound fiscal system of government. Consequently India adopted federal structure with the union of central and state governments to actualize and maintain the values of national unity, cultural diversity, regional autonomy and rapid socioeconomic transformation. The Indian Constitution has assigned the powers of the centre and state governments into three lists; a Union list, a State list and a Concurrent List. However, the third layer i.e. the local self government has been accorded recognition only after 73rd and 74th Amendments of the Constitution passed in 1993.

Under this fiscal system, the fiscal performance of central governments remained comfortable till 1980. But there was a significant deterioration in the fiscal situation in 1980s, especially by the second half, due to rapidly growing public expenditure as compared to growth of public revenue which was marked by high and persistent fiscal deficits. This large fiscal deficit had some spill-over effects on the external sector which was reflected in the widening current account deficit in the early 1990s. This necessitated a comprehensive fiscal reform programme to raise revenue and compress expenditure. The central government started the fiscal reform process in 1991 which became a continuing process thereafter too. Several fiscal reforms were made by the central government to raise revenue which mainly targeted taxation front in 1990s and 2000s, to curtail expenditure by introducing Expenditure Reforms Commission very late in 2000s and to reduce the
debt burden in mid-1990s by reducing the difference between the interest rate on market borrowings and other internal liabilities (small savings, provident funds, etc.).

In this study an effort has been made to analyse the fiscal performance of central government of India with reference to fiscal reforms.

FINDINGS

The findings that came out from this research work can be summed up as follows:-

1. Indian economy faced stern economic crisis in 1990-91. So, in order to improve the state of affairs the economic reform package was introduced in 1991-92. Fiscal reform was the key component of the economic reform programme which targeted tax reforms, expenditure reforms, systemic reforms in borrowing process of the central government and fiscal reform initiatives of the state governments. Fiscal reforms process was mainly started with the main focus on taxation reforms. Important tax reforms undertaken by the central government from time to time relate to the reduction in the highest marginal tax rate and in the basic rate of the corporate tax. Besides, central commodity taxes, i.e., union excise duty and custom duty also underwent salient changes. In the case of custom duty, there were drastic reductions in the tariff rates across the rate categories including the peak rates. In the case of union excise duty, a wide ranging and systematic effort to minimize the incidence of taxation on inputs was undertaken through the introduction of MODVAT (1987) which was further converted into a uniform rate called CENVAT.

2. Other important reforms that have been brought about since 1991 are the introduction of service tax (1994), abolition of securities transaction tax and fringe benefit tax. Reforms also entailed reduction in the rate categories and exemption regimes, throughout the period.
Efforts to curb expenditure growth through the Expenditure Reforms Commission (2000) are however late by one decade since the fiscal reform process was initiated. Numbers of policy changes are also made to activate internal debt management policy by introducing market operation in regard to absorption of Government of India dated rupees securities and longer term Treasury bills. Another reform in borrowings' process was the reduction of the difference between the interest rate on market borrowings and other internal liabilities.

3. An analysis of the basic structure of Indian taxation system, which used the data from 1950-51 to 2007-08 revealed that in central taxes, on an average, revenue from direct taxes outnumbered the indirect taxes and in states taxes, the indirect taxes are more prominent as compared to the direct taxes. However, the share of indirect taxes has increased substantially during the period under study. As the Indian tax structure has many sub parts, so an analysis has been done using t-test for independent variables. In the present study, t-test has been used to test the significance of the difference between two mean values. The following null hypotheses have been taken:

1. $H_0 = \text{There is no significant difference between All India Direct Taxes (TOTALD) and All India Indirect Taxes (TOTALIN).}$

2. $H_0 = \text{There is no significant difference between Central Direct Taxes (CENTRALD) and Central Indirect Taxes (CENTRLIN).}$

3. $H_0 = \text{There is no significant difference between States’ Share in Direct Taxes (STATESHD) and States’ Share in Indirect Taxes (STATSHIN).}$

4. $H_0 = \text{There is no significant difference between Central Net Direct Taxes (CENTRNTD) and Central Net Indirect Taxes (CENTRNTI).}$
5. \( H_0 \) = There is no significant difference between States’ Own Direct Taxes (STOWND) and States’ Own Indirect Taxes (STOWNIN).

6. \( H_0 \) = There is no significant difference between States’ Direct Tax Revenue (STTAXD) and States’ Indirect Tax Revenue (STTAXIN).

The t-analysis performed resulted into the rejection of all the null hypotheses, thereby proving that there is significant difference between various pairs of taxes taken for the analysis. The various hypotheses taken were mainly aimed at comparing the direct and indirect component of various pairs. The rejection of all the null hypotheses gave a very strong preliminary evidence of the fact that in Indian taxation structure, significant differences exist as per the nature of the taxes.

4. To know the effect of tax reforms on various sub parts of the tax revenue, regression analysis has been used. The only independent variable taken here is dummy. The cut off year of reforms is taken as 1990-91. In all, 18 regressions have been run and the results gave a very rosy picture of the reforms as the t-value has been found significant at 5 percent level of significance in all regressions.

5. The percentage of gross union tax revenue remained at the same level of around 10 percent in 1990-91 as well as in 2007-08. However, in between these two years, a lot of ups and downs have been noticed. The smoothest upward trend has been noticed in case of corporation tax followed by the income tax. On the other hand both the indirect taxes showed a declining trend particularly after 1996-97, when the Government took a decision to reduce these duties substantially to give a boost to the production and
trade activities. In the beginning of reform years, union excise duty and the custom duty were the highest contributor, however, in the later years, their contribution reduced significantly.

6. In 1990-91, union excise duty and custom duty were at the top end contributing 42.57 and 35.85 percent respectively. This contribution reduced significantly to 30.25 and 20.45 percent respectively in 2007-08. It is very much clear that the share of union excise duty and custom duty reduced continuously and significantly while the share of income and corporation tax increased over the reform period taken in the study. It highlights the changing philosophy of the Indian taxation system where a shift has occurred from the indirect taxes to the direct taxes. It further has policy implications for the equity considerations in the economy as the tax system is becoming more progressive.

7. The government introduced a service tax in 1994 in line with the recommendations of the Chelliah Committee. Starting with three services, viz., namely telephone, stock broking, and insurance services, the coverage has progressively widened over the years with about 104 services having been brought within the ambit of taxation till to date. A few important services brought under the service tax net are banking and other financial services, management consultants, credit rating agencies, and market research agencies. Some important services that are still outside of the tax net are legal consultancy services, transport of goods by waterways, and cosmetic or plastic surgery. Collections from service tax have shown a steady rise from 1994–1995 (0.04% of GDP) to 2007–2008 (1.07% of GDP).

8. In income tax and corporation tax, the tax buoyancy is less than 1 in 1990-91. Union excise duties shows tax buoyancy below 1
continuously, however, no particular trend has been found in custom duties. Similar is the case with the gross union tax revenue. However, since 2002-03, all the direct taxes show a consistent trend of better tax buoyancy. It is a reflection of the fact that tax collections in direct taxes follow the growth pattern in India. On the other hand, tax buoyancy in indirect taxes is reducing continuously during the study period. It may be the result of the various reform measures taken in various direct and indirect taxes by various committees.

9. The aggregate analysis of tax revenues of union and states revealed that in 1990-91 the indirect taxes were the larger share of aggregate tax revenues. As the reforms started showing their impact, the share of indirect taxes in aggregate tax revenue went down substantially. From 1990-91 to 2007-08 the share of indirect taxes in total tax revenue reduced 26.42 percent. This reduction was due to the asymmetric performance of the major central taxes. The union excise duties and custom duties slowed down in terms of growth relative to GDP growth while the direct taxes like income tax and corporation tax accelerated in terms of growth relative to GDP growth during the same period. However, even after this shift in relative performance, the contribution of the indirect taxes in total taxes remains larger than what it was in the early fifties (1950-51= indirect taxes shares was 63.16 p.c). This is a well known fact that the incidence of taxation is easier in the case of direct taxes. The heavy dependence of India’s tax system on the indirect taxes does not support the case for rating the design of India’s tax structure as of high quality. Furthermore, as the indirect taxes have started showing falling buoyancy in the later years of the study period, growth in the
overall tax-GDP ratio has been stalled. Reduction in the custom duty rates as part of WTO commitments, reduction in union excise duties as part of overall rationalization of the tax regime, changing of GDP structure in favour of the services whose tax potential has not been fully utilized, increase in evasion due to lack of information coordination activities etc. are some of the reasons cited for a decline in the performance of the central indirect taxes. It is difficult to say here, which of the reasons is most important, but they may all have contributed to the erosion in the buoyancy of indirect taxes. It is notable that even though tax rates were reduces in case of direct taxes, their tax buoyancy improved as the augmentation in the tax base overtook any negative effect of the reduction in the tax rates.

10. An important finding is that coefficient on log of per capita GDP is significantly positive. This is in line with other studies that found that the capacity to collect and pay taxes increases with the level of development (see for example. Our results also suggest a strong negative and significant relationship between agriculture share and revenue performance. This relationship could work through both the supply and the demand side. On the supply side, if a large part of the agriculture sector is subsistence, then this sector may be hard to tax.

11. We also find that foreign aid has a positive effect on revenue performance, but the relationship appears weaker than that for some other variables. Gupta et al. (2004) had already pointed out that if foreign aid comes primarily in the form of loans, then the burden of future loan repayments may induce policymakers to mobilize higher revenues. However, aid in the form of grants may create a moral hazard problem if it decreases incentives to
increase the tax base. We found that debt is negatively related with revenue performance, although the relationship is not very strong.

12. Our results for the institutional factors are mixed. We do not find a significant effect from the variables that capture government stability, corruption, and law and order. However, across some specification, the impact is significant when institutions are measured by political and economic stability.

13. We also investigate how the various sources of tax revenues affect the share of central government revenue in GDP. We find that taxes on goods and services as a source of revenue have lower revenue performance. Since most of the taxes on goods and services are indirect taxes, they tend to be regressive in nature. As a result, they may exacerbate the inequality in income distribution and reduce the tax base, which in some cases may result in a reduction in the share of revenue in GDP. In contrast, greater reliance on taxation of income, profits and capital gains appears to improve revenue performance. To the extent that these taxes are progressive, they reduce income dispersion and generate higher revenue. We also find that the share of tax revenue from trade does not affect revenue performance significantly.

14. Finally, revenue performance does not appear to be determined significantly by corporate and individual tax rates, or by average tariffs, once we have taken into account the structural variables, institutional variables and various sources of tax revenue. A high R-square, a low standard error and the value of Durbin Watson also proves that the regression model is, on the whole, a good fit.

15. The study found a clear trend of declining capital expenditures, mirrored in the rise of the share of revenue expenditures. There is
a degree of compulsion in the revenue expenditures as salary payments, pensions, and interest payments are all in the nature of committed expenditures. It is possible to say that revenue expenditures have crowded out capital expenditures. Revenue expenditures as percentage of GDP remained marginally above 21 per cent until 1997-98. After that year, there is a sharp increase. This is often attributed to the impact on salary payments following the recommendations of the Fifth Central Pay Commission. It is also due to the mounting debt of the central and state governments and high cost of borrowing.

16. To capture the effect of TIME and REFORMS on the Combined Revenue Expenditure of Central and State Governments, regression analysis has been used. The significant t-statistic of TIME variable for all categories of expenditures shows the secular rise in Combined Revenue Expenditure of Central and State Governments. Further, the effect of reforms has been found highly significant in case of Interest payments, Defense, Pension and Medical expenditure. Only the education expenditure has been found immune to the reforms undertaken in the economy.

17. The following may be highlighted as the main trends characterizing the changes in the structure of the combined expenditures of the central and state governments.

1. The share of revenue expenditure in total expenditure has risen steadily over time. This increase has been particularly sharp in the nineties.

2. This increase in revenue expenditure has been due primarily to a rise in interest payments relative to GDP.

3. Among general services, defense expenditure has gone down in terms of relative importance in the revenue expenditures,
while the share of pensions has gone up.

4. Among social services, there has been a stagnation in the share of education and health since 1990-91.

5. Among economic services, agriculture and transport have had the larger share. Particularly, the share of power and irrigation sectors has increased.

18. The economic services have a larger share in the case of central revenue expenditures. The agricultural sector has the largest share followed by the industrial sector, transport and communications, fertilizer subsidies, and power, irrigation and flood control. In 2007-08, the share of industry was 3.6 per cent and that of transport and communications also at this level. The fertilizer subsidies had a share 2.2 per cent in centre's revenue expenditure in 2007-08. The share of agriculture was 5.6 per cent in 2007-08 which have risen from 4.3 per cent in 1990-91. The regression results also show the significant rise in this share.

19. The main trends characterizing the expenditure profile may be summarized as below:

1. Revenue expenditures have a large share in the centre’s total expenditures.

2. This has been driven largely by the rise in interest payments, which claimed in 2007-08 nearly 34 per cent of centre's revenues expenditures.

3. Social services do not have a large share in centre's revenue expenditure profile. The largest sector within the social sector is education.

4. Among the economic sectors, agriculture has the largest share, but industry and minerals, transport and communications are also quite important.
5. The transport and communications head has witnessed a sharp rise since the early nineties.

20. Linear multiple regression equation is employed to identify the socio, economic and political constraints of public expenditure. In all 13 regressions have been run. The presence of reforms in the significant exogeneous variables list indicates the impact of reforms on all the dependent variables in this regard.

21. We find fiscal imbalance in the central government, as indicated by fiscal, primary, revenue and budgetary deficits from 1991-92 to 2007-08. The latter half of the 1980s saw gross fiscal deficit in the range of 2 to 5 per cent of GDP and gross primary deficit and revenue deficit in the range of -.93 to 3 per cent of GDP and 1 to 4 per cent of GDP, respectively. As a per cent of GDP, gross fiscal deficit was 5.55 per cent, gross primary deficit was 1.49 per cent and revenue deficit was 2.48 per cent during 1991-92. Fiscal consolidation was hence a major focus of the reform process introduced in 1991-92. The 1990s have also seen varied performance in the deficit indicators. The period 1991-92 to 1996-97 with the exception of 1993-94 has seen a decline in the fiscal deficit through a combination of an increase in revenues coupled with a reduction in expenditure and other deficit indicators as a percentage of GDP. From 1997-98, expenditure started rising once again and by the year 2001-02, all the major deficit indicators, viz., revenue deficit, fiscal deficit and primary deficit rose to levels higher than those prevalent at the beginning of the reform process. With the Fiscal Responsibility and Budget Management Act (FRBMA), 2003 in place since 2003-04, not only the gross fiscal deficit as a proportion of GDP declined, but a commensurate decline in the revenue deficit was noticed.
leading to a marked improvement in the quality of deficit. This fiscal correction in the central government since 2003-04 has been achieved on the strength of higher revenues. Success in containing or managing expenditure has been limited.

22. The public debt of the central government has been continuously increasing in India since 1975. Public debt of the central government of India increased from Rs. 27393 crore in 1975-76 to Rs. 2897037 crore in 2007-08. The reliance on borrowing increased substantially in 1980-81. This larger recourse to borrowing was facilitated due to various factors such as the availability of non-recurring receipts like the IMF loan and special bearer bonds. To meet its expenditure commitments the reliance on borrowed funds rose to Rs. 268193 crore in 1989-90. Total public debt, as a whole, registered a sharp increase from Rs. 27393 crore in 1975-76 to Rs. 268193 crore in 1989-90 - registered the growth of 18 per cent per annum. Increasing dependence on borrowings to meet the deficit on revenue account has led to a continuous growth in the total indebtedness. However, an increase in debt puts pressure on interest payments which in turn necessitates a further build up of debt. It rose from Rs. 354662 crore in 1991-92 to Rs. 2897037 crore in 2007-08 – showing therein the growth of 14 per cent per annum during the post-reform period.

23. Internal liabilities, as a component of public debt, registered a sharp increase from Rs. 19904 crore in 1975-76 to Rs. 239850 crore in 1989-90 – recorded the growth of 20 per cent per annum during the pre-reform period of fifteen years. The major contributory factors were oil shocks and political expediency.
24. Further, external debt of the centre has increased substantially from 1975-76 to 1989-90 – showing the rate of growth of 10 per cent per annum during the pre-reform period of fifteen years. It was due to the financing of large current account deficit that emerged since the beginning of eighties through inflow of capital from abroad by way of multilateral and bilateral assistance, commercial borrowing and non-resident deposits.

25. Public debt of the central government, as per cent of GDP, has increased continuously throughout the study period. This shows that fiscal measures adopted by the central government in 1991 could not help much to curtail the rising trend of its debt-GDP ratio. As per cent of GDP, internal liabilities registered a sharp increase since 1975 and reached to 59 per cent in 2007-08. On the other hand, external debt declined continuously and reached to 2 per cent of GDP in 2007-08.

26. The share of internal debt of the central government was much higher than other liabilities throughout the study period. However, the share of internal debt has shown a decreasing trend in comparison to the increasing share of other liabilities in total internal liabilities of the central government of India till later half of 90s. Recently, internal debt constitutes two-third of the total internal liabilities.

27. It can be concluded here that during 1980s, major part of loans was in the form of long term debt but since 1990, this trend has changed with the shortening of market borrowings from long term to medium and short-term debt. Now, India is moving towards balanced maturity pattern.

28. It is clear that the financial burden of debt is more than national income during whole study period resulting in restricted outlay
for the current activities. Therefore, it is necessary for the government to take some concrete steps to keep the debt GDP ratio low. It can be done by framing such policies so that income generation is promoted and debt burden be restrained to the maximum extent.

POLICY IMPLICATIONS

1. On the lines of trend in developed as well as developing countries, tax rates have been reduced in India both in the case of personal income tax as well as tax on corporations. The existing rates are competitive and are at par with other nations. Before effecting a further rate cut, it is necessary that all exemptions and deductions are eliminated. Reduction in rates will produce rational results and will help in increase in collections only when the exemptions and deductions are eliminated/abolished. Strong case for eliminating the deductions and exemptions from the statutes exists, with the reduction of the corporate tax rate and with effective reduction in personal income tax rates over the last two years. It is required that all tax preferences which lead to significant revenue loss and economic distortions are eliminated completely.

Tax breaks are inefficient and costly instruments of public policy. They fail to promote the objectives meant to be served to any significant extent. On the contrary they entail loss to revenue which remains often un-quantified and thus unknown. In many countries while tax rates were reduced in course of tax reforms, there was complete elimination of incentives and deductions from the rule book as well. For example, in Indonesia while the maximum tax rate was reduced to 35%, all the so-called incentive provisions were also withdrawn.
Elimination of exemptions and deductions shall serve as an effective measure for widening the tax base. However, bringing in a large number of potential taxpayers into the tax net is a real task before the tax officials. Tax gap continues to be large and the personal income tax is not able to capture its entire potential. At present only about 3% of 1 billion of Indian population is under personal income tax net. Attempt should be made to identify the potential taxpayers and bring them on tax records. To achieve this, it is necessary that tax department in India does have complete information about all tax assesses. The department in India has already adopted Permanent Account Number in this direction, which may also serve as Citizen Identification Number for other agencies. External sources of information, particularly corporate bodies and all government agencies should be tapped to detect entities that should be on tax records. Tax Information Network which has become operational may be effectively used for this purpose. Effective use of PAN and Tax Information Network together may help considerably in identifying the potential assesses and widening the tax base. Along with widening the tax base, effective implementation of PAN and TIN will also help in evolving required base for Risk Intelligence Network.

Presumptive taxation may be another way of widening the tax base as well as enhancing the tax collection. A successful presumptive tax should serve primarily to prepare small businesses for self-assessment and secondarily to enhance revenue. Presumptive methods are not only simple, but they can also be used for efficiency and equity goals. Apprehensions are often raised that a) problems are encountered in selecting factors
that should form the base of a presumptive income tax b) there is likelihood that the presumptive tax will tend to be shifted in an arbitrary and haphazard manner and c) there is possibility that the use of presumptive techniques will actually discourage the keeping of books and records. But there is a need that exists in developing countries for simple methods to tax the hard-to-tax groups that escape income taxation at present. Presumption offers a way by which substantive base-broadening can be achieved in developing countries because of their economic structure and because the information vacuum in which tax administration in these countries are forced to function. Some of the areas/assesses where presumptive taxation may be applied include mini bus operators, bus operators, taxi operators, self-employed persons, tuition agencies and vendors not keeping any fixed establishment. Presumption based upon outward signs of lifestyle will be effective tool in tackling tax evasion in India; more so with Annual Information Returns now providing enormous set of data about high spenders.

4. Broadening of tax base can be achieved significantly by bringing agricultural income under tax net. To begin with, major farmers or farming units may be asked to file returns of income under regular rules of taxation, whereas small agricultural units should be subjected to a simple scheme of presumptive taxation based on area, general quality and location. In order to detect new assesses, the tax department should also conduct careful scrutiny of Annual Information Returns (AIRs). Information about high spenders must be captured through AIRs and they should be brought on tax records.
5. Net under TDS may be further widened. At present, individuals and Hindu Undivided Families are exempted from the responsibility of TDS in a number of transactions. TDS may be made applicable in case of individuals and Hindu Undivided Families as well. The reason for this is the fact that in many cases the firms take shelter of these entities by creating incomes in their names to evade the provisions of TDS. Further, TDS compliance by those entities whose incomes are exempt from tax, which are loss making and large government departments may be monitored periodically. Other areas which should be monitored may include payment of airing charges to TV channels for broadcast of programmes, commission paid by airline companies to travel agents, payment of fees by hospitals, medical institutes to consultant doctors and payments by media companies in form of commission to advertising agencies. To widen the tax base, TDS may be extended to following other areas;

2. Amount paid in respect of value addition by the manufacturers.
3. Lease rent or rent on machinery and plants and debited to the accounts of a concern.
4. Market fees paid during purchase and sale of agricultural produce and debited in books of any concern.
5. Royalty paid on account of publications.
6. Incentives in whatever name; in kind or cash paid on account of extra sales or bringing extra business.
7. Payment made on account of repairs of machinery and plants.
8. Payment on account of franchises.
9. Payment in form of gifts taxable as income in the hands of recipients.

6. Tax collection machinery needs to be strengthened to recover massive tax arrears. In this direction, one major attempt should be to get taxpayers to file returns accurately and on time, while reducing the manual workload involved so that resources can be redirected to the relationship and compliance activities. Simultaneously, tax payers should be made to pay tax by the due dates, payments be processed quickly and accurately, payments be accounted for correctly and all outstanding dues be pursued without delay. As a measure of collection of regular demand following measures need to be taken:

1. Each jurisdictional office should have adequate infrastructural facilities. The jurisdictions should have adequate number of vehicles for the purpose of facilitating movement of the tax inspectors to collect taxes.

2. Suitable incentives need to be given for collection of taxes to the Tax Recovery Officers.

3. Taxpayers should be given incentives for early payment of regular demand like non-levy of penalty or reduced penalty.

4. Appeals may be decided quickly within a time frame.

5. Taxpayers must be allowed to prefer appeal only when at least 50% of the tax is paid and proof for payment is produced.

7. There is necessity of inspiring voluntary compliance by effectively detecting and prosecuting non-compliance. Aim should be to
discover misstatements in filings, accounting mistreatments in taxpayers' books and other anomalies directed towards preventing leakage from the tax net. Concept of blue returns as it exists in Japan needs to be introduced in India as well. In Japan blue return system is intended to improve tax payers' book-keeping and encourage honest self-assessment. Special privileges are granted to taxpayers who are allowed to file blue returns. A taxpayer who has income from business, real estate, or timber and who keeps proper accounting records may file a blue return if he or she submits an application by 15th of March and obtains the approval of tax authorities by the end of that year. Once a taxpayer obtains approval, he or she is entitled to file a blue return for all subsequent years. The Director of the Tax Office approves the application on the condition that the taxpayers' books are kept in accordance with the official requirements. Such system may be replicated in India as well.

8. Since tax policy is akin to tax administration, reforms are necessary which would evolve a modern system of tax administration. Poor state of tax administration has been a major reason for low levels of compliance and high compliance costs. Given the complexity in the tax structure and poor information system, the tax system often assumes the character of negotiated payments. Tax administration will prove its effectiveness if it is able to cope up with shortfall in key areas viz; unregistered taxpayers, stop-filing taxpayers, tax evaders and delinquent taxpayers.

9. There should be all round efforts to provide a consistent, seamless service across the taxpayer life cycle. The relationship with taxpayers may be based on the idea of 1) bringing taxpayers into
the system, 2) investing time in the relationship to help them understand how to be compliant and 3) maintaining the relationship over the long term. For bringing improvement in tax administration, refund procedures should be streamlined and anti-corruption machinery must be strengthened. Regular post facto sampling and review of appeal cases may be one mechanism to guard against discretion and improve tax administration.

10. Information technology may provide the tax department means to manage its manual workload and direct resources to service and compliance activities. However, information technology should not be implemented in isolation from other areas of improvements. Interactive channels shall provide benefits both to taxpayers and the tax department and thus be introduced. Internet portals that enable taxpayers to see their tax accounts, file returns and make payments, give taxpayers extended service hours and greater convenience while reducing the workload for the tax department need to be adopted. Pre-populated or pre-filled returns may reduce taxpayer's compliance burden and also reduce administrative costs. Countries like Denmark, Sweden, Norway, Estonia, Iceland and Finland have successfully adopted this practice. The pre-populated tax returns may be posted on internet and the taxpayer may be given specific time to respond. If the response is not received within the stipulated time then the tax department may take action accordingly; either raising demand or sending refund electronically. In case the return is accepted as such, the taxpayer will get the intimation electronically. Mobile kiosks, mobile technology and field workers providing services with the relevant technology can be very effective in taxpayer services. The successful use of information technology in Spain
as part of bringing improvement in tax administration is worth emulating.

11. There should be massive investment in infrastructure in the tax department. The tax department lacks enough infrastructure facilities, which puts a dampening effect on the morale of the tax officials. If top quality service is to be provided to the taxpayers it is essential that top class facilities are available to the tax department. It would be of immense benefit to the government if more investments are made in the infrastructure.

12. It is also recommended that Central Board of Direct Taxes is given autonomy on the lines of tax administration in Canada. The Central Board of Direct Taxes may be granted administrative as well as financial autonomy while it may work overall under Ministry of Finance. While autonomy is required for independent functioning, accountability must also be enforced at all levels.

13. Tax administrators may be given incentives for bringing more assesses under tax net and on tax registers. However, in order to make the scheme meaningful it is necessary that the officers are rewarded only for those cases where the new assesses remain on record for at least three years and do not go out of tax net. Incentives may also be decided on the basis of conversion of presumptive tax assesses into regular tax assesses.

14. Success of any tax reforms will depend upon how well the executive leadership team champions the process, which includes communicating and committing to measures of success. Given that tax departments play a strategic role for the nation, they should be accountable to more strategic measures. Performance should be measured on their ability to deliver true outcomes, i.e., their ability to maximize revenue collections, minimize the
transaction burden of taxpayers, promote voluntary compliance and their capacity to manage and facilitate the fiscal policies of the nation. Defining overall performance metrics and cascading the performance metrics down to a granular is must for efficient administration. This involves a cultural change towards meritocracy and a more corporate environment. The officers and staff must be posted in the investigation wing (the wing responsible for carrying out search operations) with a great deal of caution. A committee consisting of Chief Commissioner of Income Tax, Director General of Income Tax and Director of Income Tax holding charge of investigation wing of a particular charge must select only those officers and staff to handle these posts who are known to be men of honesty, integrity and commitment. Similarly, committee consisting of Member (Investigation) of the Board, Member (Personnel), DG (Investigation) concerned and DG (Vigilance) should select officers for the post of Director (Investigation). For the post of DG (Investigation), a committee consisting of Chairman, Member (Investigation) and Member (Personnel) should be constituted.

15. Tax system should be built upon strong pillars of public relations and campaign, counselling, guidance and scrutiny. Taxpayer service and education may be made the back bone of a strong and vibrant tax system. The main purpose of taxpayer service and education is to create tax awareness among taxpayers, tax agents, employers and the other stakeholders especially on taxpayers' rights and responsibilities. Following measures are suggested in order to create a better understanding and increase confidence in tax administration among taxpayers:
1. Classes on taxes at all levels - tax officials may go to schools and talk about the importance of taxes.

2. Sponsoring school essay contests on topics related to tax.

3. Certificate of appreciation to schools contributing to promotion of tax education.

4. Setting up model tax office for tax education system.

5. Seminar for taxpayers, regular TV and radio program, TV and radio spots.

6. Publishing newspapers and magazines.

7. National tax monitors system for enhancing taxpayers' understanding of tax administration.

8. Creating tax counsel systems.

9. Special counters every day of the month to provide integrated services with senior officer's assistance made available.

10. Interactive web site.

11. Setting up of service centres and call centres with facility of direct interaction at service counters at branches nationwide.

12. Creating taxpayers' counters at shopping malls, fair grounds and other strategic places.

16. On the lines of Japanese tax administration, Indian tax administration may consider establishing a system of tax consultation machinery. In Japan, tax consultation machinery consists of three different systems: Tax Counsel Officers who are used to enhance organization and publicity activities as well as taxpayers' awareness and tax concerns, tax answer system, which is an automatic computer system that answer frequently asked questions through the internet, voice-phone and facsimiles and the co-ordination officers, who are in charge of handling complaints.
from taxpayers with co-ordination duties and also provide advice and guidance. China also has a system of taxation service hall, which is in charge of handling the consultation of the taxpayer and China utilizes the voice-phone and the internet providing the answers of tax consultation. While emphasis should be upon greater reliance on taxpayers in order to support the overall tax system built upon faith and self-assessment a criminal investigation system should be built and strengthened. A strict criminal investigation system shall go a long way in supporting accurate and fair taxation.

17. Compliance behaviour of taxpayers in a country has much to do with its community's culture. It is ultimately peer pressure that compels people to pay their proper taxes. Cultural change, however, does not come about easily or quickly. Hence there is the need for persistent efforts to create an environment that fosters such changes. Tax administration should take steps towards creating such environment, so that compliance behaviour of taxpayer can be improved.

18. A successful tax reform process would also require political leadership to mobilize support and counter special incentives. Process of reforms in India has followed a gradualist approach. The attempt to reform the tax system has been rather slow. Since 1990s steps have been taken, but they are not at desired pace. The policies of reforms have to go along with broad economic reforms. So far the reforms have been tried by adopting consensual approach. Various interest groups and pressure groups come in the way of broad based reforms. It is necessary that some drastic measures be taken to bring a changeover in the system.
19. We conclude that privatization programme is one of the most appealing answer to the question of reduction of public debt because some of the discernible key features designed in the economic reform programme such as attracting non-debt creating capital flows and de-emphasis on short-term external borrowings have been designed to led to build-up adequate resources and reduction in short-term debt. A major source of vulnerability in the Asian crisis was the large stock of short-term liabilities of banks and corporate.

20. Tight monitoring and control mechanism by the Reserve bank of India, the recent amendments in the disinvestment policy by the GOI and the capital market’s positive reactions to the PSE shares are conducive for divesting GOIs holding in the PSEs in the stock market that could fetch more revenue to the government. Since the proceeds from disinvestment are invested in building the rural infrastructure and social reform programmes, the economic life of the rural people improves. As 80% of India’s population is rural, the share of rural India’s contribution to the GDP increases and paves way for higher growth rate in GDP. Hence, “Reducing public debt is a realizable objective of privatization”. The need of the hour is to resume the privatization programme and take bold decisions irrespective of the current political compulsions. It is a matter of time that such thing happens in the near future.

21. Expenditure management through appropriate prioritization and control is important for any government. The tension between containing the deficit and providing adequate outlays for the relevant heads makes expenditure prioritization an even more important issue in India than what it is in many other countries. There is need for more schools, hospitals, roads, hydroelectric and
multipurpose irrigation projects, etc, on the one hand, and sticking to fiscal prudence on the other. One of the traditional ways of safeguarding the fiscal balance is through a strict adherence to appropriate budgeting techniques and procedures.

22. There is a strong need to adopt public expenditure management framework in India. It should take care of:

1. Macro policy framework and performance feedback needs to be indicated in advance to those who are supposed to prepare activity-wise budget estimates.

2. Activity-wise allocations particularly on non-plan expenditure items need to be discussed in necessary detail.

3. Initiate, develop and insist on cost consciousness for each major activity/program.

4. Discuss and explore 'least-cost options' with beneficiaries/target groups and professionals.

5. Integrate thinly spread activities for achieving the same objectives.

6. Improve monitoring of non-plan expenditure in terms of the need, utilization and effectiveness rather than only pace of expenditure.

7. Stakeholders, participants and beneficiaries should be associated with the monitoring process.

8. Performance budget/Reports system in the Ministries should be used for guidance at the plan formulation level.

23. To exercise control on public expenditure the following framework is proposed:

1. Devise systems for operational audit for purposes of finding out “efficiency and effectiveness” of expenditure.
2. There has to be a multidisciplinary approach to assess ‘efficiency and effectiveness’ of the program; it cannot be left to accounting personnel alone as at present.

3. Workout and establish appropriate and specific incentive systems of reward for economy and better use and disincentive for slippage in expenditure control.

4. Develop appropriate management systems for maintaining expenditure information, usable both at activity control level, as well as, expenditure control level.

24. Some of the important specific suggestions relating to expenditure management include:

1. Government may examine the feasibility of introducing a multi-year budgeting process,

2. Introduce objective methods of preparing budget estimates so as to improve the quality of budget estimation,

3. Stipulate a maximum time within which, reports of C&AG are scrutinized by Public Accounts Committee and examined by Parliament or Legislature, as the case may be,

4. Review all expenditure classifications other than revenue and capital,

5. Fully computerize cash flow management at all levels of government.

6. Another necessary reform in budgeting is, to do away with the dichotomy between 'plan' and 'non-plan' in expenditure. With the introduction of planning, budget heads have come to be divided under 'plan' and 'non-plan' and the distinction runs through all items of expenditure on revenue as well as capital accounts. Apart from creating problems in keeping the revenue
deficits and thereby fiscal deficits in control, as pointed out earlier, the distinction has had a deleterious effect on the quality of public services. Essential maintenance has been neglected as they do not come under the plan and existing assets including schools and hospitals are starved of much needed support for their running.

7. In order to improve the efficiency of public expenditure we need to have better targeted, beneficiary oriented programs and an effective monitoring mechanism. It may be mentioned that the evaluation of public programs has so far been primarily expenditure oriented. However, expenditure is not an end by itself. Evaluation of performance, in terms of achievements, related to the objective is seldom done. This needs to be remedied.