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TAXATION SYSTEM AND SERVICE TAX IN INDIA

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Introduction:

In the traditional economy, the role of the Government was limited to the maintenance of law and order the Government interference in the economy was considered unnecessary. But with passage of time the interference of the Government has become inevitable.¹ At present, various Governments have entered and are entering into a great number of public projects such as social security measures and public utilities like transport, telecommunication, power, heavy electrical atomic energy etc. By the performance of these functions the Government is protecting citizens and promoting their economic and social development and for this purpose it requires heavy expenditure. Public expenditure is ever increasing years to years with the increase of these functions in both developed and developing countries in the world. In order to meet public expenditure, the Government requires revenue from public. Raising revenue from public is known as public finance and this finance become more important in modern time.

The sole objective of public finance in every country is maximizing social welfare and economic development in desired manner and direction. The economic development activities of a nation involve two operations i.e. rising of revenue and the spending of revenue. There are several ways through which the Government can be raised revenue for public use. Taxation is one of the most important sources of Government revenue of a country.
It is also a powerful incentive or disincentives weapon to stimulate economic growth of the country.²

It is universally recognized that taxation is a multipurpose instrument for augmenting revenue from domestic source. It is also an important instrument to bring about an optimum, most efficient resource allocation so that greater savings and investments are generated in the economy; surpluses and shortage in different sectors of industries are counter acted by promoting a desirable production pattern consistent with national needs.³ It create an environment in the economy where by surpluses for export are created and evolved a structure itself having inbuilt growth potential and inherent buoyancy which aims at redistributive justice; particularly keeping in view the capacity of the people to pay. In all, taxation plays an important role in the development of economic, business, investment and social life, in any country. It has also an impact on living standards. Therefore, “the Governments, merely by exercising their power to tax, are able to transfer resources from private to public use.”⁴

India being developing country, is striving to fulfill its increasing developmental needs and needs of its people within its limited resources. For this purpose, India too particularly after independence has applied well structured taxation policy with direct and indirect taxes for the economic development with its overall objectives i.e. equity and justice. Thus, direct and indirect taxes are the most important sources of revenue of the country since independence. However, Indian tax system has undergone radical change in the line with liberal economic policy and WTO commitments of the country. Therefore, Government of India being
rationalized tax structure of the country by keeping in view the national priorities and practices followed in other countries. By this way Government of India also explore alternative sources of revenue to meet ever increasing public expenditure.

3.2 Meaning and Definition of Taxation:

The origin of the word ‘Tax’ is from taxation which means an ‘estimate.’ The word “taxation derived through the French, from ‘Lat. Taxare’, to appraise which again is connected with the same root as ‘Tangere’ to touch.” It is that part of the revenue of a state which is obtained by compulsory dues and charges upon its subject. A tax is a financial charge or other levy imposed on an individual or a legal entity by a state or a functional equivalent of state (e.g. tribes, secessionist movement or revolutionary movements).

According to Somerfeld Anderson and Brock the term ‘tax’ can be defined meaningfully as, “a non- penal yet compulsory transfer of resources from the private to the public sector, levied on the basis of pre-determined criteria and with out reference to specific benefit recovered, so as to accomplish some of the nation’s economic and social objectives.”

Seligman stated that “Tax is a compulsory contribution from a person to the Government to defray the expenses incurred in common interest of all, without reference to special benefits to be conferred.”

According to the Dictionary of Modern Economic Taxation, “Taxation means compulsory levies on private Individuals and organization made by Government to raise revenue to finance
expenses on public goods and services and to control the volume of private expenditure in the economy.\textsuperscript{11}

Thus, it can be inferred from the above definitions that a tax is generally levied to augment the public revenue which is utilized for public benefit and it cannot be predicted as to what extent the amount paid by an individual to the state come back to him in the form of services rendered by the authority or state. In short, the philosophy behind such taxation is that society should itself pay for its development. Taxation, however, should not be such as to burden on an individual beyond his capacity to pay.

**Purposes of Taxation:**

Taxation has four main purposes i.e. the “4Rs”\textsuperscript{12}

1) **Revenue:**

Taxation is usually by for the most important source of government revenue. Taxation raised revenue to spend on welfare and developmental activities of the society and on more indirect functions of government like good regulation or Justice Systems. This is most widely known function.

2) **Re-distribution:**

Normally, re-distribution means transferring wealth from richest sections of society to poorer sections. This function is widely accepted in most of the democratic countries, although extent to which this should happen is always controversial.

3) **Re-prising:**

Taxation is reprising i.e. taxes are levy to address externalities to discourage bad habits and advocates many people regarding certain polices of the nation.
4) **Re-presentation:**

Taxation indicates degree of accountability and efficiency of governance. Direct taxes generate the good degree of accountably and better governance, while indirect taxes have smaller effects. This purpose of taxation is the most fundamental effect of taxation, but it is often ignored.

**Canons of Taxation:**

The taxation is one of the major sources of Government revenue. At the same time, it has got a special role in redistribution of income and reduction in inequalities of income prevailing in the society. In order to achieve to such objectives, the taxation system should be such that it is acceptable by general public, fair to all members of the society, simple to operate and capable of yielding optimum revenue. In this regard, canons of taxation lay down general guidelines for evaluating taxation system. Adam Smith, the well known economist gave us the most important canons of taxation.\(^\text{13}\)

The four normative requirements of a good taxation system lay down by him irrespective of the circumstances of different countries. These are as follows:

1) **Canon of Equity:**

According to Adam Smith “The subject of every state ought to contribute towards the support of the Government as nearly as possible, in proportion of their abilities i.e. in proportion to the revenue which they respectively enjoy under the protection of the state.”
Equity means ‘ability to pay’. This is most commonly acceptable principle of taxation. It states that the distribution of the burden of taxation should be commensurate with taxpayers’ ability to pay tax. Those who are more able to pay tax should pay more tax. The taxpayers’ ability to pay tax is measured in annual income earned by him.

Kaldor, observed that from the point of view of equity, the most important consideration is that the tax system should not contain a systematic bias in favour of particular group of taxpayers and against others.¹⁴

2) Canon of Certainty:

Adam Smith observed that “The tax which each individual is bound to pay ought to be certain and not arbitrary. The time of payment, the manner of payment, the quantity to be paid ought to be clear and plain to the contributor and to every other person.”

As per this principle, the amount tax, the time of payment, the method of payment etc must be clear, to the tax payers and tax authorities so that uncertainty is avoided. The canon of certainty was mainly advocated to prevent exploitation of tax payers by the authorities in collecting taxes. If the taxation policies are arbitrary and full of doubts and confusion, the possibility of harassment to the tax payers by the collecting authorities by using their powers can not be ruled out. In order to avoid such a situation, the taxation policies should be very clear and should create confidence in the minds of tax payers and at the same time tax being collected from them is just and proper.
3) Canon of Convenience:

This canon relates to the procedure adopted for collecting taxes. According to Adam Smith “Every tax ought to be so levied at the time or in the manner in which it is most likely to be convenient for the contributor to pay it.”

As a tax imposes a burden on the taxpayer it should be imposed at such a time and in such a manner that its payment should causes least hardship or inconvenience. The principle of convenience is further promoted that if tax laws are simple and comprehensible by ordinary tax payers then the voluntary compliance should be existed in the tax policies.

4) Canon of Economy:

Every tax involves some revenue yield and corresponding cost collection. The collection cost includes the compliance costs and administration costs. Obviously, these two types of costs should be as low as possible. Adam Smith noted that, “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 brings into the public treasury of the state.”

This canon indicates that the taxes should be imposed in such a way that the revenue from them should considerable and at the same time, the collection charges should not be too much and too high as a proportion of the total tax revenue.

International studies have found that, both administrative costs and compliance costs are higher for direct taxes than for broad based consumption taxes.15
With the passage of time, some more canons of taxation have been added to the Adam Smiths for maxims.

5) **Canon of productivity:**

It is also known the canon of fiscal adequacy. According to this, the tax system is able to yield enough revenue for the treasury so that the Government may not be required to face financial difficulties such as fiscal deficit. Thus, tax system should be capable to provide sufficient revenue to the state to perform its functions satisfactorily.\(^\text{16}\)

6) **Canon of Diversity:**

According to this, tax system should have enough tax variety so that every class of citizens may be called upon to contribute something to the state revenue. It means that there should be a multiple tax system rather than a single tax system. This will enable the state distribute the burden of taxation widely on the entire economy without causing much harm to anyone.\(^\text{17}\)

7) **Canon of Simplicity:**

According this canon the tax policy should easily understood by tax payers i.e. its nature, its aim, time of payment, method and basis of estimation and should all be easily followed by each tax payer. Obviously, the canon may remove several difficulties of the tax payer and it is in the interest of convenience. In short, tax system should simple to understand and easy to operate.\(^\text{18}\)

8) **Canon of Neutrality:**

According to the neutrality rule, taxes should not interfere with consumer’s choice and it should promote an efficient allocation of scarce resources of the economy. The spirit of
neutrality principle requires minimum interference in the working of a competitive market. In all, tax system should be such that there should be minimum possible distortionary effects on individual choices and it should allow the invisible hands of market forces to achieve Pareto optimally.\textsuperscript{19}

9) Canon of Expediency:

Canon of Expediency implies that the possibility of imposing a tax should be taken into account from different angles i.e. its reaction upon the tax payers and the society at a large. Sometimes it is seen that a tax may be desirable and may have most of the characteristics of a good tax but the Government may not find expedient to impose it. Thus this canon is of vital importance in democratic countries.\textsuperscript{20}

10) Canon of Buoyancy:

Another requirement of a good tax system is the relatively high degree of responsiveness of tax yield to changes in national income. This canon is more important particularly in developing countries, where the Government sector plays a predominant role in the development process.

Tax revenue may change through the automatic response of the tax yield to changes in national income and or through. The imposition of new taxes, or the rates of existing taxes or other administrative measures are called as discretionary changes.\textsuperscript{21}

The variations in the tax yield flowing from combined effect of automatic responses as well as discretionary changes are known as buoyancy of tax.\textsuperscript{22} This canon assesses the overall success of
government measures to increase tax revenue. In short, tax policy should be as buoyant as possible to increase tax revenue.

11) Canon of Elasticity:

With the constant tax parameters automatic changes in the tax yield resulting from variations in the national income measure elasticity of a tax system. It is the ratio of percentage change in tax revenue to the percentage change in national income. In absence or weakness of elasticity of the tax system, Government will have revised tax rates and tax base every year to keep the share of tax revenue in the national income undiminished. Such frequent changes complicate tax laws; reduce administrative efficiency and political inexpediency Therefore, the tax structure should be such that to impart reasonable degree of elasticity of the tax system.

12) Canon of Economic Stabilization:

As per this canon, it may be interpreted that the tax system should be promised full employment and if possible a stable financial level. The stabilization of the balance of payment is subsidiary objective of a well organized tax system of a country. This canon is the most important principle of a tax system in any developing country.

13) Canon of Co-ordination:

Co-ordination is an orderly arrangement of a group effort to provide unity of action in the pursuit of common purpose. In democratic countries taxes are imposed federal and local governments. It is therefore, very much desirable that there must be co-ordination between the different taxes that are imposed by different tax authorities. The constitution of India provides various
guidelines in respect to taxation by various governments in order to avoid any conflict or dispute between Central and State governments and to ensures maximum co-operation. Any government should not encroach upon the rights of other government in the matter of taxation.  

After having the explanation of various requirement of a good tax system, it is concluded that there is no country in the world which has such an ideal taxation system. Hence, the taxation system in general must become a part of economic organization of the society and should fit in its economic philosophy.

**Taxation Structure in India:**

Initially, tax structure of India was designed by the British government, incidentally for serving the purpose of raising the revenue and remotely reducing the inequalities of income. But after independence, it was found that the tax structure was being inadequate for meeting the challenges of planned economic development of a country, Therefore, Government of India, has carried out various reforms several times in the tax structure.

In 1950, India adopted, ‘Federal Government System’ through the constitution. It provides three tiers Government system comparing the Union Government, the State Government and the Local Governments. The Local Governments i.e. Urban or Rural Local Bodies are functioning directly under the control of the State Governments. Hence, the local Governments does not have separate identity in relation to allocation of powers especially for taxation. The constitution of India distributes in details the subject matter of laws that may be enacted by the Union and the legislatures of the States.
Article 265 in the constitution specifically states that, no taxes shall be levied or collected except by the authority law. Entries 82 to 92B of list-I in the Seventh Schedule refer to the taxation powers of the Union Government. Entries 45-63 of the List-II in the same schedule specify the taxation powers of the States Governments. List-III does not contain any head of taxation, which means the Union and the States have no concurrent powers of taxation. The absence of joint occupancy of tax field is meant to avoid duplication in tax administration and minimize tax rivalry between the Central and the States and among the State themselves. The residual powers of taxation, as in general legislation, belong to the Union vide entry 97 of List-I in the Seventh Schedule.

In accordance to the provisions of the Indian Constitution, the main taxes/ duties that the Union Government empower to levy are income tax (expect tax on agricultural income which the State Governments can levy), Customs duties, Central Excise, Sales Tax (Tax on Inter-State sale of goods\(^{28}\)), and Service Tax. The principle taxes levied by the state Governments are Sales Tax (Tax on Intra-State sale of goods\(^{29}\)), Stamp Duty (Duty on transfer of property), State Excise (Duty on manufacture of alcohol), Land revenue (Levy on land used for agricultural or non agricultural purposes), Duty on Entertainment and tax on Professions and Callings.

The Constitution of India does not provide any taxation powers to local governments. However, the States on their own may assign any of the taxes in the State list to the local bodies. Accordingly, the Local Bodies are empowered to levy tax on properties (Buildings etc) Octorio (tax on entry of goods for use/
consumption within the areas of local bodies), Tax on markets, Tax on user charges for utilities like water supply, drainage etc.

**Tax structure in Indian:**

Tax structure refers to the various taxes that constitute the tax system of a country. Different taxes levied under the tax system of any country can be classified on the basis of type of tax base, tax rates, tax incidence etc. Classification of taxes on the basis of tax incidence is considered more important to know the relative roles of different taxes in a country at any given point of time because the impact of relying on a particular tax may different from relying on another tax.  

Indian Tax system comprises mainly two types of taxes i.e. Direct Taxes and Indirect taxes.

**Direct Taxes:**

Direct taxes are those, which the taxpayer pays directly from his income and wealth etc. According to J. S. Mill, “A direct tax is demanded from the very person who, it is intended or desired should pay it.”

In other words, direct taxes are those which are levied immediately on incomes and property generated by individual persons or group of persons. The income of the person or the group of person is directly assessed and the tax payable is determined. This tax is directly paid by the individual to the Government treasury, out of his pocket because he is legally responsible for the payment of tax in relation to income or wealth.

In short, direct tax is that tax, which is directly levied and collected by the departments from earners of income such as
income tax and wealth tax etc. Direct taxes generally inconvenient but they are preferred because they can be related to ability to pay, satisfy the principle of certainty and create civic consciousness.\textsuperscript{32}

**Indirect Taxes:**

Indirect taxes are those, which are levied on products or services at the stage of manufacture, sale/import. These taxes are collected at the consumption stages and at the time of spending the income.

In the words of J. S. Mill, “Indirect taxes are demanded from one person in the expectation and the intention that he shall indemnify himself at the expense of another.”\textsuperscript{33}

Indirect taxes imposed on goods and services, the incidence of which is borne by customers who ultimately consumed the goods or services. In short indirect taxes are those which are imposed on goods or services rather than on persons or organizations. They are indirectly collected from customers, importers, exporters and service providers, e.g. Customs Duty, Excise Duty, Entertainment Tax, Sales Tax or VAT etc.

Indirect taxes (also called as hidden taxes), are inconvenient to collect and lack of equity attribute. In India there are series of tax laws and regulations in order to control the indirect taxation, which can either laws made by Central Government or even can be State specific laws. As a result, these taxes are an important part of the total cost. It is thus, essential to make appropriate planning for such costs.

Indirect taxes are also form major part of Governments revenue both at a Central as well as State of India. Hence, they
have great significance in the Indian tax structure even in global era; can affect every link in supply chain both domestically and internationally. This is because one person’s sale is another’s purchase and one country’s export is another’s import.  

**Different taxes levied under tax structure in India:**

The following are the major taxes levied under the tax structure in India:-

1) **Direct Taxes:**
   - Personal Income Tax
   - Tax on Corporate Income
   - Wealth Tax
   - Capital Gain Tax
   - Central Sale Tax
   - Professional Tax

2) **Indirect Taxes:**
   - Excise Duty
   - Customs Duty
   - Service Tax
   - Security Transaction Tax
   - Taxes Levied by State Governments, such as State Excise, Stamp Duty, Land Revenue, and Entertainment Tax etc.
   - Taxes levied by local authorities, such as Octorio, Tax on water supply utilities, drainage and sewage utilities, Property tax etc.
   - Other taxes.
Historical Perspective of Taxation:

The history of taxation dates back to immemorial and it is not recent development by any account. The origin of the word “Tax” is from taxation which means an estimate which is as old as civilization. A thorough research on the history of taxation system shows that taxes were levied either on the sale and purchase of merchandise or livestock and were collected in a haphazard manner from time to time.\(^{35}\)

Further, the history of taxation suggests that process of levying and the manner of tax collection were unorganized. But taxes were collected by all historical leaders and head countrymen to run its authority i.e. ruling Government machineries, to meet their military and civil expenditure and also meet the common needs of the citizens like maintenance of roads, construction of Government buildings, and administration of justice and other functions of the region.

Although, there were no homogenous tax rate structures but it depended on the production capacity and commodity of that particular country and or region. However, the tax rates and quantum were varied according annual production. As again, these taxes were collected in cash or in kind in relation to the type of commodities or services. Sometimes, the taxes were collected in kind to store with Government as buffer stock to meet emergencies. The history of taxation also suggests that the taxes were levied on all classes of citizens such as actors, dancers, singers and even on workers. These were paid in the form of gold coins, grains, raw materials and even by rendering personal service.\(^{36}\)
After having the introductory background, it is worthwhile to review the history of taxation in the following manner.

**Taxation during Ancient India:**

In India, the tradition of taxation has been in force from ancient times. It finds its references in many ancient books like “Manusmriti” and “Arthasastra.” There was a perfect admixture of direct and indirect taxes and they were varied in nature.

Manu, the ancient sage and law giver stated that “the king should levy taxes according to sastras.” He wisely advised that taxes should be related to the income and expenditure of the subject. He laid down that traders and artisans should pay $\frac{1}{5}$ part of their profit in silver and gold, while the agriculturists were to pay $\frac{1}{6}$, $\frac{1}{8}$ and $\frac{1}{10}$ part of their produce depending upon their circumstances. However, he also suggested that both extremes should be avoided namely either complete absence of taxes and exorbitant taxation. Thus, ‘Manusmriti’ clearly shows the existence of a well planned taxation system even in ancient time.

In 300BC the well known treatise on state crafts known as ‘Arthasastra’ written by Kautilya. (Known as Chhanakya and Vishnugupta) deals with the system of taxation in a real elaborate and planned manner. In Kautilyas’ time, taxes were collected as a part of the agricultural produce, which was normally $\frac{1}{6}$ and also taxes were levied as water rates, octroi duties, tolls and customs duties. At that time salt tax was an important source of revenue levied at the rate of 5%, which on liquor at the rate of 10% and general import duty was 20% ad-valorem.
The Kautilya described in details, the different types of taxes in the interest of the Mauryan Empire in order to promote trade and commerce as follows:

“Merchandise external (Bahyam i.e. arriving from country parts) internal (Abhyantram i.e. manufacture inside forts) or foreign (Atithyam i.e. import from foreign countries) shall be liable to the payment of toll alike, when exported (Nishkarmya) and imported (Praveshyam).” Imported commodities shall pay 1/5 of their value as toll and tax on pilgrims (Yatavetana).³⁹

Kautilya gave so much importance to public finance and taxation system in his Arthashastra. According to him, “The power of the Government depended upon the strength of its treasury.” He further stated that “From the treasury, comes the power of the Government, and the Earth whose ornament is the treasury, is acquired by means of Treasury and Army”.⁴⁰

The learned author K. B. Sarkar commends the system of taxation in ancient India in his book as follows:

Most of the taxes of ancient India were highly productive. The admixture of direct taxes with indirect taxes secured elasticity in the tax system, although more emphasis was laid on direct tax. The tax structure was broad based one and covered most people within its fold. The taxes were varied and large variety of taxes reflected the life of a large and composite population.⁴¹

**Taxation during Mughal Period:**

With the advent of the Mughals in India the country witnessed a sea change in the taxation system of India. During the period of 1296-1316, Sultan Alauddin Khilji introduced three taxes
on peasantry such as “Kharaj” (tax on cultivation), ‘Charai’ (tax on milk cattle) and “Ghari” (tax on houses). Further, the successor of the Sultan Khilji, Ghiyansuddin Tughluq made some alteration in his tax structure by introducing few concessions to ‘Khots’ and ‘Muqaddams’. The “Ghari” and “Charai” taxes were stopped by Firoz Tughluq and he introduced the levy of ‘Jeziya’ with some fiscal concessions. The “Jeziya” was a Islamic poll tax on non Muslims. Before this time, the land tax was known as ‘Jeziya’ or ‘Kharaj Jeziya’ and no separate other separate tax was prevalent over and above the land tax. But Firoze Tughluq imposed “Jeziya as a separate tax on the peasantry. He was also collected “Haqq-I-Shrub (a water tax)1/10th of produce the villages served by canons.

In fact, Babar, the founder of the Mughal rule in India had no tax policy as such. To quote “Babar did not even have an orderly tax system, plundering was his main source of state income, and he wrote very frankly in his diary that, he had decided to advance on an area to the west of Agra at a time when he needed money, because there were some pickings left for him there.

In October 1528, he had to levy a tax on his Amirs of 30 percent of their salaries, since he had given away every thing in India and did not have enough funds at his disposal for war equipment gunpowder and the operation of cannons.

Actually, land revenue by far was the most important source of a income for the Mughal rulers. While other taxes like gifts, import and export duties and Jizya (or Zazia) were levied in order to lining the emperor’s treasury.
The original ‘Jizya’ abolished by Akbar and it was introduced by Aurangzeb in 1679, in the form of a digressive income tax. The tax sums of such ‘Jizya’ were express in ‘Dirhams’\(^{46}\), in accordance with the words of the ‘Shariah’. For the levying the ‘Jizya’ a special service with new collectors of taxes was created. This service was led by high officials who had to control the collection of ‘Jizya’ in regular manner. “It is not known how much the new tax yielded but that was not very important either for religious motive- encouraging ‘Hindus’ to convert to ‘Islam’- prevailed over the financial objective.”\(^{47}\)

The discriminator policy based on religion adopted by ‘Mughal’ rulers was the main factor decline the ‘Mughal’ empire after the death of ‘Aurangzeb’ in 1707. In all, taxation policy of ‘Mughals’ was guided by religious consideration and it can be cleared from the following quotation:

“In the large market cities, in the sea harbours and at the borders of the empire, import and export duties of 2.5 percent advalorem were levied, later on ‘Aurangzeb’ doubled this percentage for ‘Hindus’ who had to make use of ‘Muslim’ friends to evade this taxation. There were monopoly on some goods for instance on salt and saltpeter. The monopoly on indigo yielded a few million rupees to the treasury.”\(^{48}\)

**Taxation during British Rule:**

The taxation system in modern India was developed by the British rulers during the colonial period through various legislations. The 19\(^{th}\) century show the establishment of British rule in India.\(^{49}\) The tax system in British India reflected the characteristics of traditional, agricultural economy. Revenues of
central Government were dominated by custom duties as domestic requirements for manufactured goods were met by imports chiefly from and other commonwealth countries. Import duties levied on almost all items of import where as major items subject to export duties were jute and tea in which India enjoyed in the world market.\textsuperscript{50} For this purpose British India formed the first board of revenue in Calcutta. In 1808 a new Board of trade was established for the regulation of trade.

The uniform Tariff Act was introduced in 1859 throughout the country. Several revisions in the custom policy and tariff took place during subsequent years, through such revisions were mainly related to the textile products.\textsuperscript{51} However to enactments such as Sea Customs Act, 1878 and the tariff Act 1934, were the main for the imported goods.

Besides the customs another important source of tax revenue for the Central Government was excise duty levied on few commodities. Further, the Government enacted the Indian Salt Act, 1882 to levy tax on manufacture of salt. After salt, fine cotton yarn was another commodity, which came under the levy of excise in 1894. Excise taxation in its mordent form dates back to the Act 1894, when for the first time a duty at the rate of 5 per cent ad velorem was imposed on cotton yarn of more than 20 counts.\textsuperscript{52} Excise at the rate of 6 annas\textsuperscript{53} per imperial gallon was imposed on motor spirit in 1917.

The first Income Tax Act, was introduced by British Government in February, 1860 in order to fill up the treasury which was suffered due to acute financial difficulties consequent on the freedom of 1857. Thereafter, there were many developments
were made in British India and these were generally modeled on the pattern on taxation system existing in Britain at the relevant time.\textsuperscript{54} Accordingly new levies were imposed from time to time on other items like cloth (1896), Kerosene (1922), Silver (1930), Pneumatic Tyres and Tubes (1931), Sugar matches, Steel ingots and mechanical lighters (1934) and Vegetable products (1943), Cigarettes (1944) etc. by passing separate Acts.

Later on a new tax was introduce in the year 1917 known as super tax which was subsequently replaced by the Super Tax Act, 1920. The super tax Act, 1920 and the Indian Income Tax Act, 1918 were consolidated in to Indian Income Tax Act, 1920 and which was finally came in to existence as Income Tax Act, 1961.

As per as the indirect tax was concern excise and customs were the main taxes in British India. However, each of these was levied on different items in relation to separate enactments.\textsuperscript{55} In 1944, all about 16 individual excise Acts were consolidated and Central Excise and Salt Act 1944, was enacted, which has been renamed in September 1996, as the Central Excise Act, 1944 and Central Excise Rules 1944. Similarly the provisions relating to sea, air and land customs and Indian Tariff Act 1932, were consolidated and Customs Act 1962, was enacted followed by Customs Tariff Act 1975.

The present day tax structure of India finds its roots in the first draft of Indian taxation system which was incorporated in 1922. The first draft was amended no of time according to the economic policy requirements. The present day tax structure is again in the way of repealed by the Goods and Services Tax to be introduced in 2010.
Taxation during Post Independence Era:

Indian people after getting independence adopted the constitution where by India become a sovereign democratic Republic and the Government assumed the responsibility and role of a welfare state instated of being merely a governing state. Hence, in the post independence era taxation was used as an instrument for reducing private consumption and transferring resources to the Government to an effort for economic development. Since Independence, there was a basic stress on few things like protectionism, import substitution, industrialization a large public sector, business regulation, state intervention in labour and financial markets and central planning. So that the economy of the country shifted from predominantly agriculture, forestry, fishing and textile manufacturing in 1447 to major heavy industry, telecomm-unications and transformation industries. In this direction, the approach of the Government was changed and different tax reforms were carried out in the taxation system by appointing several committees and commissions.

The first comprehensive attempt at reforming tax system was made by the Taxation Enquiry Committee 1953-54 (Chairman John Matthai). The commission reviewed the structure of taxes on income and carried out in-depth studies of the central taxes and their administration, recommended widening and deepening the tax structure, both at central and in the state level. After the revue undertaken by Nicholas Kaldor, Government of India, found that the prevailing taxation system in India was inefficient and inequitable. Accordingly as per the recommendations of Prof. Kaldor, Government of India, broaden the tax base through the
introduction of an annual tax on wealth, the taxation of capital gains, a general gift tax and personal expenditure tax, despite of this, tax collection failed to improve.

With the began of the recommendations of Taxation Enquiry committee, more and more commodities manufactured in India, including industrial inputs and capital goods were brought under the preview of Excise duties unless specifically exempted. In the year 1980, the customs revenue was brought about by a rise in the volume of imports as well as successive hikes in the import tariffs and highest rates. Tax reforms undertaken since beginning of 1999s were aimed at moderating the detrimental effect of Excise and Import duties on Economic growth. Till the year 1999 indirect taxes has dominant in the tax revenue of Central and State Governments in India.

Although, there was some decline in the share of indirect taxes of the Centre in the first of half of the 1970’s. Thereafter, it is increased to around 84 per cent in the year 1991. Government of India was made several reforms direct and indirect taxes but problem like non transparency, tax evasion and Cascading efforts of the tax structure were not ruled out. Recognizing the need for substantial reforms, the Government of India introduced MODVAT (Modified Value Added Tax) in March 1986, which was considered as major step towards simplifying the excise duty structure. Further, it was replaced with CENVAT.

**Taxation in a new era of liberalization:**

Tax reform efforts prior to 1991 were focused on enhancing revenue productivity to finance large development plans and promoting equity. Since 1991, tax system in India under gone
radical change in line with liberal economic policy and WTO commitments of the country.\textsuperscript{56} Hence, reforms were initially undertaken as a part of structural reforms such as reduction in Excise and Customs duties, lowering corporate tax, widening of tax base and toning up the tax administration.\textsuperscript{57} These reforms were aimed at augmenting revenues and removing anomalies in this tax structure through restructuring, simplification and rationalization of both direct and indirect taxes drawing mainly from the recommendations of tax reform committee 1991 (Dr. Raja Chelliah Committee). Introduction of service tax in 1994, according to recommendation of tax reform committee is an indirect tax reform had a landmark in the history of taxation. After 1991, the need for tax rationalization was the focus of various committees appointed by the Government of India. The Committees in 2001 and 2002, i.e. Dr. Parthasarathi, Dr. Y. V. Reddy and Dr. Vijay Kelkar recommended the withdrawal of tax concessions and exemptions to widen the tax base. Since 1986, the efforts were initiated towards introduction of VAT at the state. But the VAT at state level was introduced from April 2005. It is a major milestone in moving to a VAT regime at state and national level.

After the implementation of VAT successfully in the pursuance of the liberalization agenda, India now looks forward for a broad based reform in the economic setting of the country. The Government of India announced few years back its desire to transform the existing scenario of both direct and indirect taxes towards the liberalization agenda. Accordingly Government of India has set April 1, 2010 as a target date for implementation of GST. The proposed reform will be the biggest tax reform in the history of taxation on the milestone base of VAT.
History of Service Tax

Service tax was being collected in India since from 3000 years ago for a plethora of services some of them being ferry tax, betting tax, courtesans, and many others. Present Service tax commenced its journey way back in 1994, when Dr. Manmohan Singh was the Finance Minister. It has indeed attained its adulthood at a time when Dr. Singh is the Prime Minister of the country.\(^{58}\)

It is not as if those services were not taxed in India. Luxury tax, Amusement tax etc. are all forms and various manifestations of service taxes. It is also said that few years after independence, there was a tax on passenger fares. In fact, a levy of service tax in the year 1994, was an off shoot of the recommendations made by Dr. Raja Chelliah committee was back in the early 1990. The committee observed that, the indirect tax at the central level broadly neutral in relation to production and consumption of goods and should in course of time cover commodities and services. The committee failed that the country should move towards full-fledged VAT in due course covering services and commodities.

In this record the committee recommended charging of tax on services on the pattern of advanced economies. The purpose of service tax is to broaden the tax base augment revenue and enhance participation of citizens in economy development.\(^{59}\)

Since 1994, the service tax net has been widening further by roping in more number of services over the years. Similarly the rate of service tax is increased every year. But it is reduced from 12 percent to 10 per cent in the year 2009. The importance of service tax is growing from its inception and it can be perceived from the
steady increase in the yield of revenue collection, mainly from metro cities and bigger towns. However, service tax unfortunately, has not seen healthy growth in terms of a strong legal framework. In the short run, it has registered stunning growth in the revenue mop up (from Rs. 410 crore in 1994 to Rs.51133 Crore projected in 2008). But its long term growth has been compromise for the lack of evaluation of the law.\textsuperscript{60}

In all, service tax is the tax of 21st Century and it growing as adult and being ready to merged in to Goods and Services Tax to be implemented in 2010.

**Goods and Services Tax (GST)-A New perspective of Taxation.**

In recent years, the Government of India has undertaken significant tax reform particularly in indirect taxation system. This includes region based and state level VAT on goods. After successfully carried through the second generation of economic reforms in accordance with the liberalization agenda, taxes still forms a barrier to interstate and international trading.\textsuperscript{61} In order to attain a secured market for the activities related to service and goods, India now look forward for a broad-based reform in the economic setting of the country. Towards this agenda, the Government of India announced few years back its desire to transform the exiting scenario of both direct and indirect taxes.\textsuperscript{62}

On the direct tax side, the Ministry of Finance made public its ongoing task of rewriting the Income Tax Act, towards simplifying the law that exits and to broaden the tax base as suggested by the Kelkar Committee (i.e. task force on Direct Taxes) while in case of indirect tax regime, the then Finance Minister, Mr. P. Chidambaram went a step ahead than that
suggested by the Kelkar committee (task force on Indirect Taxes) and made clear the intention of the Government to adopt a harmonized system of taxation relating to goods and services.\textsuperscript{63}

In the Union Budget of, 2006-07, Finance Minister proposed that, India would operate a Goods and Service Tax w.e.f. 1\textsuperscript{st} April, 2010 and then postponed up to 1\textsuperscript{st} April 2011, that would be shared between Centre and the States.

The GST is being levied in one from or the other in 140 countries. Their experience suggests that the GST can function in a reasonably satisfactory manner in developing countries. Thus, GST system is targeted to be a simple, transparent and efficient system of indirect taxation. This involves taxation of goods and services in an integrated manner as the blurring the line of demarcation between goods and services and has made separate taxation of goods and services untenable.

The Finance Minister has been announced in his Budget speech, that GST would be implemented from April, 2011. This is good for India because, the GST will create a single, unified Indian market to make the economy stronger. However, there are still uncertainties regarding its implementation including levy and collection, rate, pattern and so on.

Accordingly, the researcher would like to highlights certain aspects of the proposed GST in India.

\textbf{Need and Importance of GST:}

It is well recognized that, the Indian taxation system particularly indirect taxation is more complex having number of laws and regulations. However, it is predominant taxation regime
and garners more revenue collection to the country. Therefore, Government of India has undertaken significant reforms in indirect taxation system but the system of taxation of goods and services till not become nation wide, simple transparent and efficient one. In this context, the Kelkar Task Force has suggested a comprehensive GST based on VAT principle. Accordingly, India is planned to implement GST system. Since, it is one of the biggest reforms in India to integrate State economies and boost overall growth. In this direction the need and importance of GST in India will arises because of the following reasons.

1. Service sector is growing very faster than the other sectors and contribute more than half GDP of the country but services are not taxed appropriately.

2. Indian economy requires a world wide simple and transparent system of taxation for the effective execution of free trade agreements as signed by it.

3. The present system of taxation leads to greater complexities in administration and compliance since, there is no splitting of transactions value in to the value of goods and services for taxation.

4. The present tax GDP ratio of India being very low and it causes various distortions in the economy.

5. The present tax structure is not overruled from cascading effects even in the system of value added tax.

**Meaning of GST:**

Goods and Services Tax (GST) is a comprehensive levy of tax on manufacture, sale and consumption of goods as well as
services at a national level. It is collected on value added goods and services at each stage of sale or purchase in the supply chain through a tax credit mechanism.

The system allows the set-off of GST paid on the procurement of goods and services against the GST which is payable on the supply of goods and services. However, the consumer at the end in the supply chain bears this tax.

Experts say that “GST is likely to improve tax collections and boost India’s economic development by breaking tax barriers between States and integrating India through a uniform tax rate.”

The major highlights of the scheme of GST as per the white paper issued by Empower Committee and changes therein from time to time are given below

**Nature of GST:**

The proposed GST will not be an additional tax. Its structure in India consists of dual levy-

1. **Central GST:** Under CGST taxes at the Central level such as Central excise duty (i.e. CENVAT) service tax and additional duties of Customs shall be subsumed.

2. **State GST:** Under SGST taxes at the state level like value added tax, Central sales tax, entertainment tax, luxury tax, octroi, lottery taxes, electric duty, state surcharges related to supply of goods and service and purchase tax shall be subsumed.

Thus, it will be a dual GST system will be levied on the taxable value of transaction. All goods and services with few
exceptions will be brought into the GST net. There will be no distinction between goods and services for the charging of tax.

**Rate of GST:**

The tax will be collected in three tiers rates. During the first and second year **GST on goods** will charged in two rates i.e. **Goods at lower rate** for necessary items and goods of basic importance, **Goods at standard rate** for goods in general. Rates of **GST on service** will remain same from the beginning.

<table>
<thead>
<tr>
<th>Year</th>
<th>Categories</th>
<th>CGST</th>
<th>SGST</th>
<th>Total GST</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011 April</td>
<td>Goods at lower rate</td>
<td>6</td>
<td>6</td>
<td>12</td>
</tr>
<tr>
<td></td>
<td>Goods at standard rate</td>
<td>10</td>
<td>10</td>
<td>20</td>
</tr>
<tr>
<td></td>
<td>Services</td>
<td>8</td>
<td>8</td>
<td>16</td>
</tr>
<tr>
<td>2012 April</td>
<td>Goods at lower rate</td>
<td>6</td>
<td>6</td>
<td>12</td>
</tr>
<tr>
<td></td>
<td>Goods at standard rate</td>
<td>9</td>
<td>9</td>
<td>18</td>
</tr>
<tr>
<td></td>
<td>Services</td>
<td>8</td>
<td>8</td>
<td>16</td>
</tr>
</tbody>
</table>

From the third year i.e. April 2013, if everything is going according to planning, and there is no much Burdon of compensation (to State Govt.) on central government the tax rate will be reduced and there will be only two rates for goods and services:

<table>
<thead>
<tr>
<th>Year</th>
<th>Categories</th>
<th>CGST</th>
<th>SGST</th>
<th>Total GST</th>
</tr>
</thead>
<tbody>
<tr>
<td>2013 April</td>
<td>Goods at standard rate</td>
<td>8</td>
<td>8</td>
<td>16</td>
</tr>
<tr>
<td></td>
<td>Services</td>
<td>8</td>
<td>8</td>
<td>16</td>
</tr>
</tbody>
</table>

**Taxable events:** In GST Taxable events are supply of goods and supply of services, any economic events which is not supply of
goods is considered as supply of services, a service provider or trader has to collect tax in two element called CGST (For Central Government) SGST (for State Government) and paid separately.

**Scope of GST:**

All the goods and services will be covered under the GST net. But alcohol, tobacco, petroleum products are likely to be out of the GST regime.

**Threshold limit for GST**

The exemption limit of GST has been proposed to 10 Lakh Both for services and goods. So any business with a turnover below 10 Lakh will be exempted from levying GST. Current threshold for excise duty is 1.5 crore, so more manufacturers liable for GST this will help to compensate state government lose to an extent.

**Exempted Goods**

All the exempted goods under VAT remain exempted under GST also.

**Input Tax Credit System:**

Input tax credit of central GST shall be allowed to be for utilized for payment of CGST only and ITC of State GST can be used for payment of State GST only. Cross utilization will be allowed except in cases of interstate supply of goods and services under Integrated goods and Services (IGST) model.

**Implementation of GST:**

Introduction of GST, essentially require extensive consultation between the Centre and States. It has been decided that the Empower Committee of State Finance Ministers shall work
with the Central Government to finalise the roadmap for introduction of GST. The Empower Committee has constituted in May 2007.

The Empower Committee is likely to finalize the details of GST. However, the States have to sort-out several issues like agreement on Constitutional amendments and holding talks with industrial associations. Exports feel that drafting of legislation and the implementation of law will take time.

**Interstate Transaction:**

For taxation of interstate transaction, IGST model has been proposed. In the model Centre shall levy IGST, which would be CGST plus SGST. The seller shall pay IGST after adjusting available IGST, CGST and SGST. The importing dealer shall claim credit of IGST paid. The credit from one state shall be transferred to other state using a clearing house mechanism.

**Remission/Deferments/Exemption scheme under the existing Act:**

Existing Central Excise/ Sales Tax concession scheme in the special area is likely to continue. Various schemes if needed shall be converted into cash refund scheme so that chain on input tax credit is not disturbed.

**About SEZ, EOU/STPI/EHTP etc:**

A sale to SEZ units is zero rate of GST. However, no benefits will be given to the sales from an SEZ to DTA. The white paper does not say anything about how the GST will work for EOUs, EHTPs. EOUs are also zero rated since EOUs are meant for
export of goods/services. Hence, the treatment for EOUs should be at par with SEZ as both promote exports to the country.

**GST on Imports:**

On imports of goods and services, both CGST and SGST will be levied. The incidence of tax will be based on the destination principle and tax revenue accrual to the state in case of SGST will be based on the consumption of imported goods and services. Here, there is a more ambiguity to determine which state the goods or services have been consumed to determine the revenue of the SGST.

**Administration power:**

In case of the administration power to the central GST is the Central and for State GST for State to be given. In case of amend or issues of any notifications, circulars, whether the states have been given power to amend these notifications or circulars etc. or not is still unclear.

**Constitution Amendment:**

Soon the amendment in constitution will happen to enable the State to tax the Services and Centre to Tax Goods which are hitherto restricted to the Central and States respectively.

**Conclusion:**

Taxation system is as old as civilization. It means compulsory levies imposed by a government on individuals or organizations in relation to their income, wealth or sale of commodities or services to raise revenue to meet public expenditure and to control the volume of private expenditure in the economy. The philosophy behind the taxation is that, society
should itself pay for its development but it not burden on individuals or organizations beyond their capacity to pay. It is universally accepted that taxation is a multipurpose instrument for augmenting revenue from domestic source in developing and developed countries. But there any country in the world in which has such an ideal system of taxation to encompass all canons of taxation. However, the taxation system in general, must be a part of economic organization of the society and should be fit in its economic philosophy.

The history of taxation in India is a fascinating subject. It is not a novelty in India introduced by British, as is too commonly supposed. Nor, it is the outcome of 19th and 20th century civilization as in other countries of the world. It was ancient and well known and recognized institutions in India since time immemorial.

Taxation in India particularly after independence has been applied well structure taxation policy with direct and indirect taxes for its economic development. However, Indian taxation system since from new economic policy in 1991, have undergone radical transformation, due to changing fiscal reforms of Indian government. Many new laws and Acts were being introduced replacing old laws and all related issues. As a result of such reforms, Service Tax and VAT under indirect tax regime but taxes still form a barrier to inter-state and international trading. Hence, India planed to implement GST form April 2011 to attain a secured market for the activities related to goods and services.
References:


12. “http://www.legalservice.com”-New Dimension to India’s Taxation policy


28. As per Section 3 of Central Sales Act, 1956 ‘A sale or purchase of goods shall be deemed to take place in the course of interstate trade or commerce if the sale or purchase-

1) Occasions the movement of goods from one state to another.

2) Is effected by transfer of document of title to the goods during their movement from one state to another.

29. Subject to the provisions of Section 3 said above, if sale or purchase of goods shall be deemed to take place inside a state then such sale or purchase shall be deemed to have taken place outside all other states.

30. Subject to the provisions of Section 3 said above, if sale or purchase of goods shall be deemed to take place inside a state then such sale or purchase shall be deemed to have taken place outside all other states.

31. Subject to the provisions of Section 3 said above, if sale or purchase of goods shall be deemed to take place inside a state then such sale or purchase shall be deemed to have taken place outside all other states.


37. I bid Indian Tax Info.


45. Jizya (or Zazia), is an Islamic direct tax of the nature of a pole tax in India. Under some Mughal Emperors, Zazia i.e. Capitation tax was levied on non Muslims in live of Military service which was required for all Mohammedans.

46. Dirham’ is a currency in the Aurangzeb Rule. One Dirham is equal to 25 to 27 paisa as equated in 1970.


53. One Anna was equal to $\frac{1}{16}$ of a rupee before the introduction of the metric system of currency from April 1,1957


55. http://www.indiataxinfo.com –“Taxation in India and British Heritage”

56. http://www.advamog.inc

57. http://www.economywatch.com

58. Shailendra Kumar,(2008) “Chidambaram should focus on Tax Administration,” Financial Express News, Feb.15,


64. “http://www.iloveindia.com”