



Brazil, Russia, India and China (BRIC):

**Tax system structures and the effects on development
and foreign trade performance**



BRAZIL, RUSSIA, INDIA AND CHINA (BRIC):

Tax system structures and the effects on development and foreign trade performance –
lessons and solutions

© 2011 - Agência Brasileira de Desenvolvimento Industrial - ABDI

Brazil, Russia, India and China (BRIC): Tax system structures and the effects on development and foreign trade performance lessons and solutions

Qualquer parte desta obra pode ser reproduzida, desde que citada a fonte.

Universidade Católica de Brasília

ABDI - Agência Brasileira de Desenvolvimento Industrial

CGEE - Centro de Gestão e Estudos Estratégicos

Supervisão

Maria Luisa Campos Machado Leal (Diretora)

Equipe da ABDI

Marina Pereira Pires de Oliveira (Responsável Técnico)

Projeto Gráfico e Diagramação

Via Comunicação Editora

Organizadores

Marcos Aurélio Pereira Valadão

Antônio de Moura Borges

Autores e Colaboradores

Alexander Pogorletskiy (Rússia)

Antônio Moura Borges

Arnaldo Sampaio de Moraes Godoy

Carolina Pancotto Boher

Elias Emanuel Alves de Sousa

Isaias Coelho

Ivo Teixeira Gico Junior

Lauriana Magalhães Silva

Leila Maria Da'Juda Bijos

Marcos Aurélio Pereira Valadão

Maria Dolgoplova (Rússia)

Maria Teresa Bustamente

Maurício Muriack de Fernandes e Peixoto

Maurin Falcão

Paulo Borba Casella

Vishwa Nath Alok (Índia)

Welber Oliveira Barral

Zhu Weiqun (China)

Ficha Catalográfica

AGÊNCIA BRASILEIRA DE DESENVOLVIMENTO INDUSTRIAL.

Brazil, Russia, India and China (BRIC): Tax system structures and the effects on development and foreign trade performance - lessons and solutions

Brasília: Agência Brasileira de Desenvolvimento Industrial, 2011.

402p.: il.; graf.; tab.

ISBN 978-85-61323-28-8

CDD 634.04

ABDI

Agência Brasileira de Desenvolvimento Industrial

Setor Bancário Norte

Quadra 1 - Bloco B - Ed. CNC

70041-902 - Brasília - DF

Tel.: (61) 3962-8700

www.abdi.com.br

TABLE OF CONTENTS

1. Presentation	7
<hr/>	
2. Brazil	9
<hr/>	
2.1. Globalization Effects on the Brazilian Tax System Marcos Aurélio Pereira Valadão	10
2.2. Brazilian tax system: history, perspectives and critical analysis Maurício Muriack de Fernandes e Peixoto	36
3. Russia	95
<hr/>	
3.1 The Russian Tax System and its Effects in Development and International Trade Relations: Legal and Economic Approach Alexander Pogorletskiy, Maria Dolgopolova	96
3.2. Lessons from Russian tax reform Arnaldo Sampaio de Moraes Godoy	139
4. India	141
<hr/>	
4.1. Tax system and reform in India: An analysis from the perspective of economic development and international trade Vishwa Nath Alok	142
4.2. Introduction to the constitutional law of India Arnaldo Sampaio de Moraes Godoy	203
4.3. The influence of India on global issues and its relations with Brazil (pronouncement) Leila Bijos	207
5. China	209
<hr/>	
5.1. The Chinese Tax System and its Effects in the Development and in International Trade Relations of China: A Juridical and	



4. India

4.1. Tax system and reform in India: An analysis from the perspective of Economic Development and International Trade

Vishwa Nath Alok*

CONTENTS

1. Introduction
2. Constitution and Tax Structure in India
 - 2.1. The Legislative Framework
 - 2.2. Tax Structure in India
 - 2.3. Tax Jurisdiction and Apportionment
 - 2.3.1. Sharing of Central Taxes:
 - 2.4. Intergovernmental Fiscal Transfer: The Mechanism
3. Tax System in India
 - 3.1. Direct Taxes
 - 3.2. Indirect Taxes: A Move towards Goods and Service Tax
 - 3.2.1. Excise Duty/Central VAT
 - 3.2.2. Service Tax
 - 3.2.3. State-VAT
 - 3.2.4. Harmonization of Interstate Tax
 - 3.2.5. A Way towards GST

* Indian Institute of Public Administration, New Delhi, vnalok@gmail.com

¹ I'm grateful to Rajkumar for excellent research assistance in producing statistical tables. I'm also grateful to Himanshu Gupta, S K Mohanty, and Mahesh Purohit for helpful discussions. S P Sharma and M.S. Bisht provided excellent secretarial support. Usual disclaimer applies.

- 3.3. Customs Duty
 - 3.3.1. High Tariff
 - 3.3.2. Low Tariff
 - 3.3.3. Single Rate
- 3.4. Taxation and E-commerce
- 4. Economic Development
 - 4.1. Macroeconomic Developments
 - 4.2. Total Factor Productivity
 - 4.3. The Human Development Index
 - 4.4. Infrastructure Development
 - 4.5. Foreign Investment Flows
 - 4.6. Double Taxation Avoidance
- 5. Conclusions
- 6. References
- Annexes
 - Annex 1 - Legal Structure of Major Taxes in India
 - Annex 2 - Items with above "Peak" Basic Customs Duty Rates
 - Annex 3 - India's commitments under various trade agreements till 2009
 - Annex 4 - List of Regional Trade Agreements
 - Annex 5 - Double Taxation Agreement Treaties
 - Annex table.1 - Selected macroeconomic indicators, 2000-09
 - Annex table.2 - Basic economic and social indicators, 2000-09
 - Annex Table.3 - Revenue Power of Rural Local Governments in Indian States at Each Tier

1. Introduction

The BRIC Nations viz, Brazil, Russia, India and China together account for 40 percent of the world's population and 40 percent of global gross domestic product (Table-1.1).

In recent times, the cooperation among BRIC is gradually gaining more substance with the growth in trade and investment. On June 16, 2009, the leaders of the BRIC countries held their first summit in Yekaterinburg, Russia, and issued a declaration calling for the establishment of a multipolar world order.

India is among the fastest growing BRIC economies, and plays the part in coordinating international efforts to overcome the ongoing financial and economic slowdown. In the recent past, India has witnessed high economic growth with rapid expansion in trade and outbound investment to developing countries including Brazil, Russia and China (BRC). The trend has attracted attention to international forums also. The analysis emanating from such forum emphasizes the need for long standing partnership between India and BRC.

While the India-BRC economic relationship is picking up steadily in this decade, a scenario of business uncertainty is being created after the emergence of global meltdown, which surfaced in October 2008. The symptoms of global recession are predicted to

be disastrous for the global economy. After a prolonged phase of recession, the world economy just revived, and buoyancy continued until 2007 before plunging into another episode of recession in 2008. According to IMF projections in 2008, the global output growth is likely to decline in near the future.

In such a critical situation, developed countries and emerging economies are capable of taking the heat of the recession in terms of emerging global economy to create conditions for the early recovery so that tenure of the recessionary phase for the global economy can be shortened. Less developed countries, which suffered severely during the so-called 'lost decades of growth', are likely to face the severity of the global meltdown if the present economic impasse continues for a longer period of time. This would adversely affect growth prospects of less developed economies because many of these countries resort to depend high on exports. In many such cases, export becomes a major driver to maintain high growth in the economy. Decline in the demand for global absorption may have a dampening effect on the export prospects of these economies.

Considering the high propensity of imports in developed countries, it is expected that these countries can become major part of global imports to absorb exports originating from less developed countries. Industrialized countries, however, are already in deep crisis before the eruption of full-fledged recession in the world economy. Average real growth rate of industrialized countries has already started declining much before October 2008.

The developed countries have registered sharp fall in real growth rate of GDP in 2007, and it is likely to be negative in the near future. In this situation, emerging countries such as BRIC are expected to perform better than the global average, although the fact that these economies are likely to face downturn during this episode of global recession. India, as an emerging country, is no exception to this trend. It may be noted that India posted a robust average growth rate of more than 9% during 2005-07. But growth performance is likely to go down in the near future. Despite the decline in India's growth prospects as projected by various domestic and multilateral agencies, the achievable targets for real GDP growth can project India as the fastest growing market-driven emerging economy in the world. India's major driver of growth during the period of crisis would be domestic demand as projected by IMF².

In this context, relevance of BRIC economic cooperation is important in terms of mitigating the severity of anticipated impact of global meltdown. It is believed that India is likely to grow fast during the period of crisis, over two and a half times higher than the rate of growth of global output. Since the expansion of the economy is mostly driven by the surging domestic demand, India can offer a larger market access to BRC countries.

The domestic demand for India could range from high-technology intensive products to primary products. As we can see from Table 1.2 and 1.3, India's trade with BRC has increased about ten times between 2000 and 2008.

² Mohanty, S.K. and Sachin Chaturvedi 2009.

Brazil, Russia, India and China (BRIC)

Tax system structures and the effects on development and foreign trade performance - lessons and solutions

Table 1.1. Global Rankings of the BRIC

Categories	Brazil	Russia	India	China
Area	5th	1st	7th	3rd or 4th
Population	5th	9th	2nd	1st
GDP (nominal)	10th	8th	12th	3rd
GDP (PPP)	9th	6th	4th	2nd
Exports	21st	11th	23rd	2nd
Imports	27th	17th	16th	3rd
Current account balance	47th	5th	169th	1st
Received FDI	16th	12th	29th	5th
Foreign exchange reserves	7th	3rd	4th	1st
External debt	24th	20th	27th	19th
Public debt	47th	117th	29th	98th
Electricity consumption	10th	3rd	7th	2nd
Number of mobile phones	5th	4th	2nd	1st
Number of internet users	5th	11th	4th	1st

Source: Wikipedia

Table 1.2. Contribution of India's Export to the World and BRC (Rs. Billion)

Year	World	Brazil	China	Russia	BRC Total	BRC % to total of world
2000-01	2013.6	10.2	37.9	39.7	87.7	4.4
2001-02	2090.2	10.4	45.4	38.1	93.9	4.5
2002-03	2551.4	23.2	95.6	34.1	152.9	6.0
2003-04	2933.7	12.7	135.8	32.8	181.3	6.2
2004-05	3753.4	30.5	252.3	28.4	311.2	8.3
2005-06	4564.2	48.3	299.2	32.5	380.0	8.3
2006-07	5717.8	65.8	375.3	40.9	481.9	8.4
2007-08	6558.6	90.8	434.1	37.8	562.7	8.6

Source: Centre for Monitoring India Economy (India Trade)

Brazil, Russia, India and China (BRIC)

Tax system structures and the effects on development and foreign trade performance - lessons and solutions

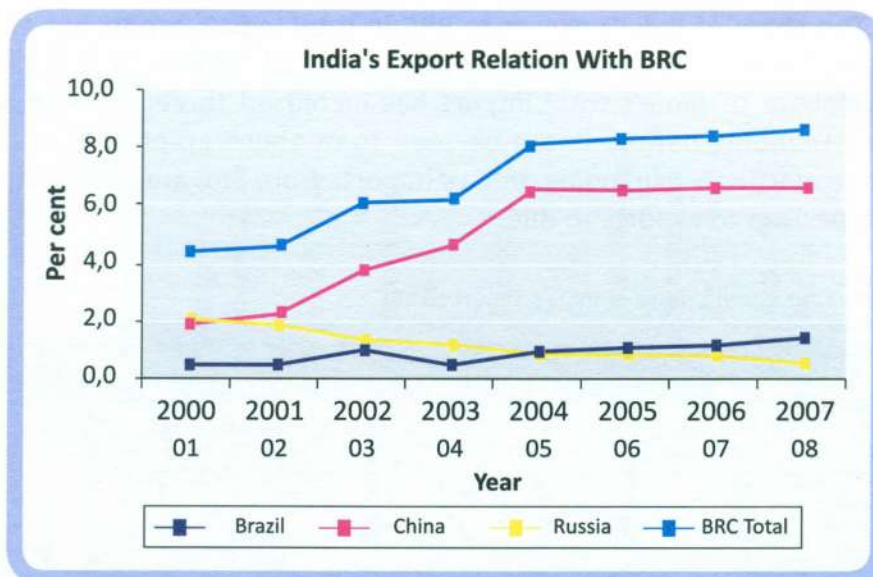
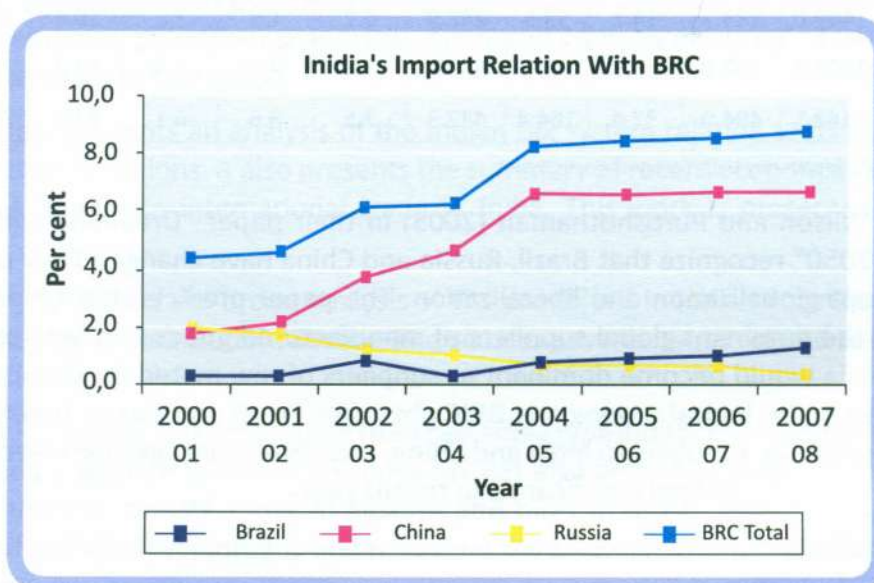


Table 1.3. Import to India from the World and BRC (Rs. Billion)

Year	World	Brazil	China	Russia	BRC total	BRC % to total of world
2000-01	2283.1	6.5	68.2	23.6	98.3	4.3
2001-02	2452.0	14.7	97.1	25.5	137.4	5.6
2002-03	2972.1	15.3	135.1	28.7	179.1	6.0
2003-04	3591.1	14.4	186.3	44.1	244.8	6.8
2004-05	5010.6	35.6	318.9	59.4	414.0	8.3
2005-06	6604.1	39.5	481.2	89.5	610.2	9.2
2006-07	8380.5	44.9	790.1	109.0	944.0	11.3
2007-08	10123.1	38.2	1090.3	99.6	1228.1	12.1

Source: Centre for Monitoring India Economy (India Trade)



2. Constitution and Tax Structure in India

2.1. The Legislative Framework⁴

In India, the executive power at the federal level is vested in the President, who is assisted by the Cabinet⁵, while legislative power is held by the Parliament. The head of the Executive, the President, is elected for five years by an electoral college comprising elected members of both the upper and lower houses of the Parliament and the state legislatures. The Vice President is elected also for a period of five years by an electoral college made up of members of both houses of Parliament. The President is aided by the Council of Ministers, which is headed by the Prime Minister. The Prime Minister is appointed by the President, who also appoints the remaining Cabinet members on the advice of the Prime Minister⁶. Members of the Cabinet must be members of the Parliament; any Cabinet member which is a Member of the Parliament for six consecutive months can continue to be a member of the Cabinet⁷.

The Parliament, comprising the President, the Council of the States (*Rajya Sabha*) or upper house, and the House of the People (*Lok Sabha*) or lower house, hold legislative power. The Council of States may have a maximum of 250 members (of which 12 are nominated by the President);⁸ It may not be dissolved but one third of its members are subject to retirement every two years⁹. The House of the People, which sits for five years, may have a maximum of 550 members, of which 530 are elected from the states and 20 from the Union Territories¹⁰.

Except for money bill, all bills may be introduced in each house; money bills, under Article 109 of the Constitution, may only be introduced in the House of the People. All bills, except bills amending the Constitution, must be passed by a simple majority in both houses of Parliament and be signed by the President in order to become law. The President may request amendments to the bill and withhold assent; however, if the bill is passed again in its original form, the President may not withhold assent. Money bills, once approved by the House of the People, must either be approved or returned to the House of the People with recommendations by the Council of States within 14 days. If the House of the People accepts the recommendations, the bill is deemed to be passed by both houses; if it does not accept the recommendations, the bill is deemed to have been passed by both Houses in the form in which it was passed by the House of the People. If

⁴ Initial part of this section is drawn from WTO, 2007.

⁵ Articles 52 and 53 of Chapter 1, Part V of the Constitution. Neither the President nor the Vice President can be members of Parliament.

⁶ Article 75.

⁷ Article 75.

⁸ Members of the Council of States include not more than 238 representatives of the states, who are elected by the legislative assembly members (elected) of each state, as well as 12 members nominated by the President (Article 80)

⁹ Each member is elected for a term of six years. Every two years, one third of these members complete their six-year term resulting in the election of one third of the membership of the Council at the beginning of every third year.

¹⁰ In addition, under Article 331 of the Constitution, the President may, if he believes that the Anglo-Indian community is not adequately represented in the House of the People, nominate not more than two members of that community to the House of the People.

the bill is not returned to the House of the People within 14 days, it is also deemed to be passed by both houses.

Under Article 123 of the Constitution, if the President sees the need to enact legislation during Parliament's recess, an ordinance may be promulgated. The ordinance has the same force as an Act of Parliament. However, it will expire six weeks after the reassembly of Parliament, unless it is enacted into law by both houses.

The Constitution also provides for a division of jurisdiction between the Parliament and the legislative assemblies of states and union territories¹¹.

The Supreme Court, head of the judiciary, consists of a Chief Justice and not more than 25 other judges. There is a High Court in each state and district and session courts happen at the district level. The Supreme Court has jurisdiction over all disputes between the Union and the states or between the states¹². It is also the final court of appeal on civil and criminal proceedings of a High Court. The Supreme Court may also, at its own discretion, grant special leave to appeal to any judgment taken by a national court or tribunal. Its decision is binding on all courts.

India's legal system is based on written law. The judiciary is independent and there is a separation of the judiciary from the executive. The system suffers from a shortage of staff, infrastructural constraints, and procedural delays. Recent efforts to address this problem include the establishment of fast-track courts to resolve criminal cases and more funding to the judicial system¹³. Other steps include a project on Information and Communication Technology Enablement of the Indian Judiciary, established in October 2005, and a National Legal Literacy Mission, in March 2005. The lower courts, however, remain weak and apparently also prone to corruption¹⁴.

In addition, to reduce the burden on the legal system and to enable quicker disposal of claims in some cases, tribunals such as Consumer Forums have been set up. An alternative form of dispute resolution, the *Lok Adalat* (courts of the people) has also helped to settle a large number of cases out of court, thereby reducing the pressure on the already overburdened legal system¹⁵.

¹¹ There are currently 28 states, 5 union territories and 2 union territories with legislature.

¹² As India is a union of states, the Constitution specifies certain responsibilities as being the jurisdiction of state governments, while others are in the jurisdiction of the Union government (the Union list) and remaining are shared. For example, issues related to international trade and international agreements are in the Union's list of the Seventh Schedule; public health and sanitation, agriculture, water and land are stating subjects; and economic and social planning, criminal and civil procedures, electricity and price controls are on the "Concurrent list".

¹³ According to Government of India 2006, some Rs 2.8 billion has been released by the Union to the state governments since 1993-94 for the development of infrastructural facilities for the judicial system (Department of Justice, Ministry of Home Affairs. Online source).

¹⁴ A study on corruption in India by Transparency International found in 2005 that, among public services, the lower courts were seen by the population to be among the most corrupt (Transparency International, 2005). India was ranked 88th out of 158 in the 2005 Corruption Perceptions Index (Transparency International, 2005). Corruption is closely related to lack of transparency and consequent scope for administrative discretion. In this regard, India ranks among the most opaque (42nd out of 48) countries based on the 2004 Opacity Index, which measures the degree to which countries lack clear, accurate, easily discernible and widely accepted practices governing the relationships among governments, businesses, and investors.

¹⁵ By 31 December 2005 almost 500,000 such lok adalats had been set up and around 18.6 million cases settled out of court.

2.2. Tax Structure in India

The Constitution makes elaborate and complex arrangements related to the distribution of taxes between the Union¹⁶ and the states, and power of borrowing and provision for grants-in-aid by the Union to the states. The underlying philosophy of these arrangements is to place adequate financial resources at the disposal of the two tiers of government to enable them to discharge their respective responsibilities under the Constitution.

Seventh Schedule of the Constitution specifies the powers between the Union and states. List I in the Seventh Schedule refer to the taxation powers of the Union government (Table 2.1). List II, in the same Schedule, specifies the taxation powers of the state governments (Table 2.2). List III, which is a concurrent list, does not contain any item related to taxation, except one related to stamp duty. In other words, the tax assignment follows the principles of separation.

Table 2.1. Taxes within the Jurisdiction of the Union as Enumerated in the seventh schedule of the Constitution of India

S. No	Entry No in List I	Description of the tax/ duty
1.	82	Taxes on income other than agricultural income
2.	83	Duties of customs, including export duties
3.	84	Duties of excise on goods manufactured or produced in India except alcoholic liquors for human consumption and narcotics but including medicinal and toilet preparations containing alcohol
4.	85	Corporation tax
5.	86	Taxes on the capital value of assets, exclusive of agricultural land, of individuals and companies; taxes on the capital of companies
6.	87	Estate duty in respect of property other than agricultural land
7.	88	Duties in respect of succession to property other than agricultural land
8.	89	Terminal taxes on goods or passengers, carried by railway, sea or air; taxes on railway fares and freights
9.	90	Taxes other than stamp duties on transactions in stock exchanges and future markets
10.	91	Rates of stamp duty in respect of bills of exchange, bank checks, promissory notes, bills of lading, letters of credit, policies of insurance, transfer of shares, debentures, proxies, and receipts
11.	92	Taxes on the sale or purchase of newspapers and on advertisements published therein
12.	92A*	Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase takes place during inter-State trade or commerce
13.	92B**	Taxes on the consignment of goods (whether the consignment is to the person making it or to any other person), where such consignment takes place throughout inter-State trade or commerce
14.	92C***	Taxes on services
15.	97	Any tax not enumerated in List II or List III of the Seventh Schedule

* Inserted by the Constitution (Sixth Amendment) Act, 1956 (w.e.f. 11-6-1956)

** Inserted by the Constitution (Forty-sixth Amendment) Act, 1982. (w.e.f. 2-2-1983)

*** Inserted by the Constitution (Eighty-eighth Amendment) Act, 2003.

Source: Government of India (2005)

¹⁶ The term "Union" and "Center" has been used interchangeably in this paper.

Service tax has been placed, after Constitution Act (Eighty-eighth Amendment), 2003, under the Union List in the Seventh Schedule under Article 268A, which reads as follows:

- 1) Taxes on services shall be levied by the Government of India and such tax shall be collected and appropriated by the Government of India and the states in the manner provided in clause (2).
- 2) The proceedings in any financial year of any such tax levied in accordance with the provisions of clause (1) shall be:
 - a) collected by the Government of India and the States;
 - b) appropriated by the Government of India and the States.

In accordance with such principles of collection and appropriation may be formulated by Parliament by law.

Table 2.2. Taxes within the Jurisdiction of States as Enumerated in the seventh schedule of the Constitution of India

S. N ^o	Entry N ^o in List II	Description of the tax/ duty
1.	45	Land revenue
2.	46	Taxes on agricultural income
3.	47	Duties in respect of succession to agricultural land
4.	48	Estate duty in respect of agricultural land
5.	49	Taxes on lands and buildings
6.	50	Taxes on mineral rights subject to any limitations imposed by Parliament by law relating to mineral development
7.	51	Duties of excise on alcoholic liquor and narcotics manufactured or produced in the State but not including medicinal and toilet preparations containing alcohol
8.	52	Taxes on the entry of goods into a local area for consumption, use or sale therein
9.	53	Taxes on the consumption or sale of electricity
10.	54*	Taxes on the sale or purchase of goods other than newspapers, subject to the provisions of Entry 92A of List I
11.	55**	Taxes on advertisements other than advertisements published in the newspapers (and advertisements broadcast by radio or television)
12.	56	Taxes on goods and passengers carried by road or on inland waterways
13.	57	Taxes on vehicles, whether mechanically propelled or not, suitable for use on roads, including tram-cars subject to the provisions of Entry 35 of List III
14.	58	Taxes on animals and boats
15.	59	Tolls
16.	60***	Taxes on professions, trades, callings and employment
17.	61	Capitation taxes
18.	62	Taxes on luxuries, including taxes on entertainment, amusements, betting and gambling
19.	63	Rates of stamp duty in respect of documents other than those specified in the provision of List I with regard to rates of stamp duty

* Substituted by the Constitution (Sixth Amendment) Act, 1956:

** The words 'and advertisements broadcast by radio or television' inserted by the Constitution (Forty-second Amendment), Act, 1976:

*** The scope of these taxes is spelt out in Article 276, the clause (2) of which fixes the amount payable by a person on account of these taxes.

Source: Government of India (2005)

The property of the Union is exempt from state taxation under Article 285(1). Likewise, the property and income of the states are exempt from Union taxes, except that Parliament may, by law, provide Central taxation of any trading activities of a state which is not incidental to the ordinary functions of state government - Article 89(2). As regards Union Territories, the Parliament has the power to impose any tax included in the state List.

Constitution also imposes certain restrictions on the taxation powers of the states. Although a State legislature enjoys the power to levy any of the taxes mentioned in List II, in the case of certain taxes, this power is subject to restrictions imposed by substantive provisions of the Constitution. Some examples of these restrictions are as follows.

The powers to impose taxes on the sale or purchase of goods, other than newspapers, belong to the state (see entry 54 of List II). However, Article 286 ensures that sales taxes imposed by the states do not interfere in imports and exports or inter-state trade and commerce, which are matters of national importance. In view of this, Article 286 places the following restrictions on the power of the states to enact sales tax legislation.

No law of a State shall impose a tax on the sale or purchase of goods where such sale or purchase takes place (i) outside the state; or (ii) during import into or export out of the territory of India;

With regard to inter-state trade, there are two restrictions: (i) the power to tax sales taking place in the course of inter-state trade and commerce belongs to the Union (vide entry 92A of List I in the Seventh Schedule), and (ii) the sales tax on intrastate sales of 'declared goods' (i.e. goods of special importance in inter-state trade) are subject to certain restrictions in terms of the nature of the levy and the rate of tax.

A State legislature is empowered to levy a tax on professions, trade, calling or employment (see entry 60 of List II). However, the total amount payable in respect of any person to the state by way of such tax is not to exceed Rs. 2,500 per year [Article 276(2)].

A State legislature is empowered to levy a tax on professions, trade, calling or employment *vide* entry 60 of List II. However, the total amount payable in respect of any one person to the state by way of such tax is not to exceed Rs. 2,500 per annum [Article 276(2)].

2.3. Tax Jurisdiction and Apportionment

Like most federations, the tax powers in India are specified by law between the Union and the constituent units, namely the states¹⁷. The powers and functions of the respective levels of government are enumerated in the Seventh Schedule to the Indian Constitution.

The concurrent list has no item that has any direct bearing on taxation except one. This relates to 'stamp duties other than duties or fees collected by means of judicial stamps, but not including rates of stamp duty'. Recovery of taxes, like any other public demands, also occurs in the concurrent list. The residual powers of taxation, as in general legislation, belong to the Union (see entry 97 of List I in the Seventh Schedule). The Union, therefore,

¹⁷ An exception is the USA, where the Constitution is silent on the assignment of indirect taxes, except tariffs (McLure, 1983).

can enter tax fields not charted in the Constitution. For example, the Union government, under such power, imposed gift tax in the past, which was abolished in 1998. Similarly, service tax was also imposed in the beginning of this millennium under such power.

Contrary to the practice in several other federations where taxes can be levied concurrently at two levels, the right to levy a given tax, in the Indian Constitution, belongs exclusively to the tier to which it is assigned. In practice, the tax arrangements of Union taxes can be classified into the following categories.

- Service Tax levied by the Union and collected and appropriated by the Union and the states (Article 268A), but does not form part of the divisible pool.
- Duties levied by the Union but administered and appropriated by the states (Article 268): e.g duties of excise on medicine and toilet preparations containing alcohol, and stamp duties on bills of exchange, etc. as mentioned in the entries 84 and 91 of the Union List respectively, and taxes on the sale or purchase of goods where such sale or purchase takes place during inter-State trade or commerce, and taxes on the consignment of goods where such consignment takes place throughout inter-State trade or commerce as per the entries 92A and 92B in the Union List.
- Taxes levied and shared between the Union and the states (Article 277): All taxes referred to in the Union list, except the one mentioned above, are levied and collected by the Government of India and from a divisible pool that is shared between the Union and the states.

Moreover, there are taxes mentioned under entries 87, 88 and 92 B in the Union List that is not being levied. These entries pertain to estate duty, and succession duty in respect of property other than agricultural land and taxes on the consignment of goods where such consignment takes place during inter-state trade or commerce. The incidence of both estate duty and succession duty is on the same object, viz. property being inherited after the death of the owner. In the case of the estate duty, the value of the whole estate, even if situated in more than one state, is the base for tax. The succession duty is related to the value of individual shares (i.e. parts of an estate) being inherited by the successors. The Estate Duty was imposed in India in 1953 and abolished in 1985.

Local governments, both rural and urban, have been recognized in the book of the statute after 1992. They have no exclusive power of taxation under the Constitution¹⁸. They derive their taxing authority from the state governments. The states on their own may assign any of the taxes in the State List to the local governments. The taxes generally assigned to local governments are property taxes, octroi, and taxes on vehicles, taxes on the professions, trades, calling license fees, etc.

Seemingly, the tax assignment in the Indian Constitution is in conformity with the theories of tax assignment in federations, "the basic scheme of the Constitution dividing the field of taxation between the Union and the states and incorporating adequate arrangements for sharing of resources between them is sound and no

¹⁸ See Alok (2006) for more details

major modifications in it are called for” observed by the Commission on Center-State Relations in 1988. From the equity and efficiency criteria, progressive income and expenditure taxes should be with the federal government. Destination-based consumption taxes like sales tax should be with the sub-national government. Local government should levy property taxes, and all three levels of government should have the authorities to collect user charges (McLure, 1983, Shah, 1994). Tax assignments mentioned in the Indian Constitution are consistent with the theoretical literature. The exception related to the power of the states to tax natural resources, such as minerals, was corrected subsequently by giving dominant power to the Union to levy or regulate the tax on minerals¹⁹.

Although the Indian constitutional scheme on tax assignment seems good on paper, its actual working has revealed many shortcomings, including the following:

Vertical imbalance: The substantial number of taxes has been assigned to the states, but the most buoyant taxes, i.e. customs, union excise, corporate income tax and personal income tax are with the Union. As a result, the Union government collects two third of the total revenue. The states together with local governments²⁰ collect the rest. Since sub national governments are assigned about two third expenditure responsibilities, it needs large fiscal transfers from the Union to state governments. Vertical imbalance is considered desirable in a federation to ensure the redistribution of income and the constitution makers deliberately made this provision but not to this degree. Initially, when governments’ budgets used to have revenue surplus and capital investments were funded through borrowings, vertical imbalance of small magnitude was justified. In the eighties, both levels of governments started showing revenue deficit and huge fiscal deficit. “The accountability suffers when revenue and expenditure decisions are declined²¹.” It erodes fiscal discipline and creates a widening vertical fiscal gap;

Tax Exportation: The Union has the power to tax central sales tax on interstate sales. It delegates the power to the state to administer the tax and retain the revenue. Under the scheme, the exporting state collects the revenue by levying central sales tax on the sale of goods from the state. The consumer of the importing state has to bear the tax. Thus, the central sales tax is the major vehicle of tax exportation and distorts the common market that the union of states in India offers.

Tax Competition: The power of sales taxation is with the States. In the past, in the absence of coordination among them, the states engaged in tax war by lowering tax rates on automobiles and electronics items to lure consumers, providing tax incentives, exemption and deferment of different kinds to encourage trade and industry in their jurisdictions. All of them led to revenue loss and distortion in the location of industries.

¹⁹ Mines and Minerals (Regulation and Development) Act of 1957.

²⁰ Local governments collect very little (Alok, 2009).

²¹ Bagchi, 1998 p 324.

2.3.1. Sharing of Central Taxes

Exclusive powers have been assigned to both, the Union and the states, but the Union cannot appropriate all the proceeds of the taxes collected by them. As per the design of the Constitution, revenue from Union taxes is required to be shared with the states to fulfill their needs.

Before 2003, only personal income tax and the Union excise duties were shared with the States. The sharing of the income tax was mandatory under Article 270 while that of the Union excise duties was discretionary under Article 272. Under tax rental arrangements with the States, the Union government collected the tax on behalf of the states and then distributed the proceeds among the states based on criteria recommended by the successive finance commissions. These were (a) additional excise duty in lieu of the sales tax on textiles, tobacco and sugar²² and (b) grant in lieu of tax on railway passenger fares.

Following the Constitution (Eightieth Amendment) Act, 2000, all central taxes have been brought into a divisible pool, and a certain percentage is shared with the states.

The article 270 is amended and provide for the sharing of all central taxes, except taxes under Articles 268 and 269 and cesses, and surcharges under Article 271. Only net revenues are shared after deducting a cost of collections.

Prior to 1988's Amendment to the Constitution, Union government levied the service tax under its residual powers (see entry 97 of List I in the Seventh Schedule), and was part of the divisible pool. It is now excluded.

In the 80th amendment, the objective was to construct a pool of all central taxes for sharing so that a holistic view could be taken, and both sides could share in the aggregate buoyancy of the central tax revenues. With service taxes being excluded from the ambit of the recommendations of the finance commission, the idea of the overall shareable pool of central taxes appears to be in the process of being reversed. While service taxes are likely to prove highly buoyant soon, these will not be subjected to share with the states under the Constitution, although other statutory arrangements can be made, which can include sharing as well as assignment. It may be noted that hitherto items under articles 268 and 269 were subjects that were generally of interstate nature, with limited revenue importance. These were wholly assigned to the States. In this context, it needs to be stressed that any legislation passed by Parliament with respect to appropriation of service tax proceeds must ensure that the revenue accrue to the states through any proposed changes should not be less than the share that would accrue to them, had the entire service tax proceeds been part of the shareable pool²³.

²² These commodities were considered to be of national importance, and the states do not levy a sales tax on these items as per the agreement, in 1956, between the Union and states,

²³ Government of India 2004, p.15-16.

2.4. Intergovernmental Fiscal Transfer: The Mechanism

“The Constitution clearly divides powers and responsibilities between two levels of governments with some amount of flexibility. “Exact correspondence of resources and functions is impossible to secure in any federal situation, but in India the balance is tilted rather heavily in favor of the Center and the outstanding feature of the financial relationship between the Center and the states. Consequently, the former is always the giver and the latter are the receivers. The favorable position given to the Center in regard to financial resources reflects the strong-Center theme running through the Constitution and many feel that this has been an important factor in keeping the country united²⁴.” Vertical imbalances between the revenue powers and functional responsibilities of different tiers of government are a characteristic feature of all federations, whose economies are large. Therefore, vertical imbalance calls for transfer of resources from federal government to the sub-national governments.

In India, wide variations can be seen in the capacity and resources across states. Thus, intergovernmental fiscal transfers are an integral part of the system. Such transfers were envisaged in the Constitution for vertical and horizontal redistribution of income. The Constitution has a simple provision. But, in practice, the fiscal transfer system in India has become quite complex and the money flows from multiple channels, including the following:

- Non-plan statutory transfers through the Finance Commission.
- Plan transfer through the Planning Commission.
- Discretionary transfer under central and centrally sponsored schemes.

In addition to these transfers, funds also flow to the States through the establishment of Central public sector enterprises, subsidized lending by financial institutions and subsidized loans to the states from the central government and the banks.

Finance Commission Transfers: It is perceived that the Indian Constitution is not a static document since it provides continuity with change. The provision of Finance Commission under article 280 illustrates this point. The Constitution does provide for central transfers, but it neither indicates the share of the states in the divisible taxes nor prescribes any principles for the distribution of taxes among the states. Thus, the percentage and manner of sharing taxes and the actual determination of grants is left to the Finance Commission. The President of India, in every fifth year or earlier as deemed necessary, appoints the Finance Commission, composed by a chairman and four members.

The Commission recommends to the President, inter alia, the principles of distribution between the Union and the states of the proceeds of taxes and the allocation among the states of the shares of such proceeds. The Finance Commission makes a detailed assessment of the financial position of the finances of the Central and state governments.

Both Union and state governments submit their memoranda to the Commission. The Finance Commission transfers a share of certain central taxes and grants-in-aid

²⁴ Administrative Reforms Commission 1968, p. 15.

of revenues to the states. In other words, although the exclusive taxation powers are assigned to both the Center and the states, yet all the taxes and duties levied by the Center cannot be appropriated by the Center. Certain taxes and duties collected by the Center are shared with the States to supplement the revenues of the states in accordance with their fiscal need and capacity. In addition, the Finance Commission also recommends grants-in-aid under article 275(1) to such states, which still need financial assistance even after the provision of shared taxes from the Union. At present, the 13th Finance Commission is set to give its recommendation before the end of the year 2009.

Planning Commission Transfers: After India gained independence, a formal model of planning was adopted. For the purpose, the planning commission, with Prime Minister of India as chairperson, was established. It was set up on 15 March, 1950, with Prime Minister Jawaharlal Nehru as the chairman. The Planning Commission has to make a periodic assessment of all resources in the country and formulate plans for the optimum utilization of resources. Below are the functions of the Planning Commission:

- To make an assessment of the resources of the country and to see which resources are deficient.
- To formulate plans for the most effective and balanced utilization of country's resources.
- To indicate the factors which are hampering economic development.
- To determine the machinery that would be necessary for the successful implementation of each stage of the plan.
- Periodical assessment of the progress of the plan.
- With the changing times, the Planning Commission is preparing itself for long term vision for the future. The commission is looking forward to maximizing the output with minimum resources.
- For being a centralized planning system, the Indian economy is slowly progressing towards indicative planning wherein the Planning Commission has set the goal of constructing a long term strategic vision for the future.
- It sets sectorial targets and provides the catalyst to the economy to grow in the right direction.
- The Planning Commission plays an integrative role in the development of a holistic approach to the formulation of policies in critical areas of human and economic development.

The financial assistance of the Planning Commission comprises grants and loans. The assistance in allocation based on a formula devised by the Planning Commission and approved by the National Development Council of which the Prime Minister is the Chairperson and the Chief Ministers of States and Cabinet Ministers are members.

Brazil, Russia, India and China (BRIC)

Tax system structures and the effects on development and foreign trade performance - lessons and solutions

Out of the total funds transferred to states, 30 percent is earmarked to special category states²⁵. These states spend the money on their own plan projects. The remaining 70 percent of the funds are distributed among 17 general category states based on a formula with weights assigned to population, per capita income, fiscal management and special problems. Previously, 30 percent of the assistance was given as grant and the remaining 70 percent was given as loans. As per the recommendation of the Twelfth Finance Commission, central loans to states have been discontinued from 2005. States are now encouraged to raise resources from the market. At present, 11th Five Year Plan is in operation.

In addition to the finance commission transfers and planning commission transfers, financial assistance is given to states for identified purposes through central schemes. Despite sharp criticism of these schemes, a large amount of funds flows through about 200 schemes. The relative importance of these transfers can be seen from Table-2.3.

Table 2.3. Fiscal Transfers from Centre to States as % of Gross Revenue Receipts of the Union Finance Commission Period Average (percent)

Year	Finance Commission Transfers			Other Transfers			Total Transfers (4+7)
	Share in Central Taxes	Grants	Total Transfers through Finance Commission (2+3)	Grants through Planning Commission	Non-plan Grants (non-statutory)	Total Other Transfers (5+6)	
1	2	3	4	5	6	7	8
VII FC	22.39	1.96	24.35	12.11	1.66	13.77	38.11
VIII FC	20.25	2.52	22.77	13.56	1.54	15.10	37.86
IX FC	21.37	3.42	24.79	14.48	1.06	15.54	40.33
X FC	21.4	2.34	23.75	10.57	0.63	11.19	35.79
XI FC (first two yrs)	20.93	5.20	26.13	10.39	0.82	11.21	37.20

Source: Government of India, 2004

3. Tax System in India

As mentioned in the previous section, the power to levy taxes in India is clearly demarcated between the Union government and the state governments. The Union government levies both direct taxes such as corporate income tax and personal income tax and indirect taxes such as customs and excise duties/CENVAT and a service tax. States levy a VAT/state sales taxes (in State where VAT is not yet in force), stamp duty, state excise, land revenue and tax on professions. State can also levy a tax on agricultural income. Local governments both rural and urban are empowered by their respective State governments to levy a tax on properties, octroi and collect user charges for utilities like water supply, drainage, etc.

²⁵ Out of 28 states in India, eleven are special category states. These states have difficult geographical terrain and considerable international borders.

Table 3.1. Fiscal Trends in India (% of GDP)

Year	Revenue Deficit (Centre)	Fiscal Deficit (Centre)	Primary Deficit	Tax Ratio (Centre)	Tax Ratio (States)	Tax Ratio (Total)
1990-91	4.2	9.3	4.9	7.6	5.3	12.8
1995-96	3.2	6.5	1.6	6.9	5.4	12.2
1996-97	3.6	6.3	1.1	6.8	5.2	12.0
1997-98	4.2	7.2	2	6.3	5.3	11.6
1998-99	6.4	9	3.6	6.0	5.1	11.1
1999-00	6.3	9.5	3.8	6.6	5.3	11.8
2000-01	6.5	9.2	3.3	6.5	6.0	12.5
2001-02	6.9	9.6	3.4	5.9	6.6	12.5
2002-03	6.6	9.3	3.0	6.5	6.7	13.2
2003-04	5.7	8.4	2.0	6.8	7.0	13.8
2004-05	3.6	7.3	1.2	7.1	7.3	14.5
2005-06	2.6	6.6	0.8	7.5	7.6	15.1
2006-07(RE)	2.1	6.5	0.9	8.4	8.1	16.5
2007-08(BE)	1.2	5.7	0.3	8.6	8.2	16.8

Source: Indian Public Finance Statistics and CMIE.

RE: Revised Estimates

BE: Budget Estimates

3.1. Direct Taxes

In the beginning, after independence in India, the direct taxes were highly influenced by the 'socialist pattern of society'. The taxes were levied to finance planned economic development. The Report of Taxation Enquiry Commission in 1954 recommended raising revenues through high rates of taxes in a progressive structure. Later, in 1956, Kaldor Committee prescribed a host of other direct taxes, i.e., expenditure taxes, a wealth tax and a gift tax to be integrated with the taxes on income, capital gains and estates. As a result, the personal income tax, in 1973-74, had eleven tax slabs with the highest rate of 85 percent above the income of Rs. 2,000,00. With 15% surcharge, the effective rate was 97.5 percent. In a way, the system encouraged people to evade taxes and generate black money. In the following two decades, there were sporadic efforts to reduce the tax rates. Finally, Manmohan Singh initiated a structural adjustment program when he became Finance Minister in 1991 and tax reform was its integral part. The Tax Reform Committee, under the chairmanship of Raja Chelliah, was constituted. As per the recommendations of the Committee, the personal income tax rates were considerably simplified with only three slabs rates of 20-30-40 percent. This was reduced further to 10-20-30 percent in 1997-98.

Brazil, Russia, India and China (BRIC)

Tax system structures and the effects on development and foreign trade performance - lessons and solutions

Table 3.2. Combined Revenue Receipts of Union and States in India (R\$ billion)

Year	1990-91	1995-96	2000-01	2005-06	(RE) 2006-07	(BE) 2007-08
GDP	5696	11918	21023	35867	41292	47234
Tax Revenue	877	1753	3053	5877	7355	8548
Direct taxes	123	358	718	1676	2310	2688
a) Corporation income tax (CIT)	53	165	357	1013	1465	1684
b) Personal income tax (PIT)	54	156	318	608	782	936
c) Other direct taxes*	15	37	43	56	63	67
Indirect taxes	755	1395	2336	4201	5045	5860
a) Customs	206	358	475	651	818	988
b) Union excise duties	245	402	685	1112	1173	1302
c) Service tax	0	9	26	231	382	502
d) State excise duty	50	87	159	264	308	331
e) General sales tax	182	357	729	1365	1665	1928
f) Other indirect taxes**	71	183	261	578	699	810

Source: Union Budgets, Indian Public Finance Statistics, and CMIE.

Note: * Other Direct Taxes includes Estate duty, Interest tax, Wealth tax, Gift Tax, Land Revenue, Hotel receipts tax, and expenditure tax.

** Other Indirect Taxes includes Stamp & registration fees, Sales tax, Taxes on vehicles, Tax on goods & passengers, Tax & duty on electricity and Other.

Table 3.3. Contribution of Each Major Tax of Centre and States in GDP (%)

Year	1990-91	1995-96	2000-01	2005-06	(RE) 2006-07	(BE) 2007-08
Tax Revenue	15.4	14.7	14.5	16.4	17.8	18.1
Direct taxes	2.2	3.0	3.4	4.7	5.6	5.7
a) Corporation income tax (CIT)	0.9	1.4	1.7	2.8	3.5	3.6
b) Personal income tax (PIT)	0.9	1.3	1.5	1.7	1.9	2.0
c) Other direct taxes	0.3	0.3	0.2	0.2	0.2	0.1
Indirect taxes	13.2	11.7	11.1	11.7	12.2	12.4
a) Customs	3.6	3.0	2.3	1.8	2.0	2.1
b) Union excise duties	4.3	3.4	3.3	3.1	2.8	2.8
c) Service tax	0.0	0.1	0.1	0.6	0.9	1.1
d) State excise duty	0.9	0.7	0.8	0.7	0.7	0.7
e) General sales tax	3.2	3.0	3.5	3.8	4.0	4.1
f) Other indirect taxes	1.2	1.5	1.2	1.6	1.7	1.7

Source: Same as table 3.2

Brazil, Russia, India and China (BRIC)

Tax system structures and the effects on development and foreign trade performance - lessons and solutions

The Corporate Income Tax rate was also reduced in a phased manner to 40 percent in 1993-94. It reduced further to 35 percent in 1997-98. Minimum Alternate Tax (MAT) was introduced to discourage zero tax companies avoiding taxes by taking full advantages of concessions and tax incentives in the tax structure. The prevailing rates and the provision of personal income tax, corporate income tax, capital gain tax and withholding tax are given in Annex 1. The fiscal importance of taxes can be seen in tables 3.1 to 3.8.

Table 3.4. Contribution of Each Major Tax in the Total Tax Revenue of the Union and States (%)

Year	1990-91	1995-96	2000-01	2005-06	(RE) 2006-07	(BE) 2007-08
Direct taxes	14.0	20.4	23.5	28.5	31.4	31.4
a) Corporation income tax (CIT)	6.1	9.4	11.7	17.2	19.9	19.7
b) Personal income tax (PIT)	6.1	8.9	10.4	10.3	10.6	11.0
c) Other direct taxes	1.8	2.1	1.4	1.0	0.9	0.8
Indirect taxes	86.0	79.6	76.5	71.5	68.6	68.6
a) Customs	23.5	20.4	15.6	11.1	11.1	11.6
b) Union excise duties	27.9	22.9	22.4	18.9	15.9	15.2
d) Service tax	0.0	0.5	0.9	3.9	5.2	5.9
e) State excise duty	5.7	4.9	5.2	4.5	4.2	3.9
e) General sales tax	20.8	20.4	23.9	23.2	22.6	22.6
f) Other indirect taxes	8.1	10.5	8.5	9.8	9.5	9.5
Total Tax Revenue	100.0	100.0	100.0	100.0	100.0	100.0

Source: Same as table 3.2

Table 3.5. Gross Revenue Receipts of the Centre (R\$ billion)

Year	1990-91	1995-96	2000-01	2005-06	2007-08	2008-09	2009-10
GDP	5696	11918	21023	35867	47234	53218	n.a.
Total Revenue	550	1100	1927	3480	5419	5622	6145
Gross Tax Revenue	430	819	1369	3662	5931	6279	6411
Direct taxes, of which	69	223	497	1623	2959	3450	3700
a) Corporation tax (CIT)	53	165	252	1013	1929	2220	2567
b) Personal income tax (PIT)	13	43	238	608	1026	1226	1129
c) Other direct taxes*	3	15	7	3	3	4	4
Indirect taxes, of which	361	596	873	2038	2972	2829	2711
a) Customs	206	358	342	651	1041	1080	980
b) Union excise duties	141	222	498	1112	1234	1084	1065
c) Service tax	0	9	20	231	513	650	650
d) Other indirect taxes	14	9	14	45	79	16	16

Source: Same as table 3.2

Table 3.6. Share of Each Major Tax in Gross Tax Revenue of the Centre (%)

Year	1990-91	1995-96	2000-01	2005-06	2007-08	2008-09	2009-10
Direct taxes, of which	16.1	27.2	36.3	44.3	49.9	54.9	57.7
a) Corporation income tax (CIT)	12.4	20.1	18.4	27.7	32.5	35.4	40.0
b) Personal income tax (PIT)	2.9	5.3	17.4	16.6	17.3	19.5	17.6
c) Other direct taxes	0.7	1.8	0.5	0.1	0.1	0.1	0.1
Indirect taxes, of which	83.9	72.8	63.7	55.7	50.1	45.1	42.3
a) Customs	48.0	43.6	25.0	17.8	17.6	17.2	15.3
b) Union excise duties	32.8	27.1	36.3	30.4	20.8	17.3	16.6
c) Service tax	0.0	1.1	1.4	6.3	8.6	10.4	10.1
d) Other indirect taxes	3.2	1.0	1.0	1.2	1.3	0.3	0.2
Gross Tax Revenue	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Same as table 3.2

3.2. Indirect Taxes: a Move towards Goods and Service Tax²⁶

At present, the move in India is towards comprehensive goods and service tax by integrating primarily Union Excise Duty, State Sales Tax and Service Tax. As mentioned earlier, the Indian Constitution assigns Union Government to impose a broad spectrum of union excise duties (UEDs) on production or manufacture of goods and the state governments the power to levy a tax on sale of goods. The authority to levy a tax on services has been assigned to the Union List. However, the states are empowered to levy a tax on some services through entertainment tax, electricity duty, motor vehicles tax, passengers and goods tax, entry tax, octroi etc.

3.2.1. Excise Duty/Central VAT

Excise Duty/CenVAT is levied by the Union Government at the manufacturing level on almost all manufactured goods except hydrocarbon and tobacco. The Union government initially levied Union Excise Duty (UED) on about a dozen articles at a very low rate of tax. However, as the time passed by, the rates were revised and the tax base was enlarged to bring more items into the tax net. It was levied mainly on finished goods but also covered raw materials, intermediate goods and capital goods. The first reform in the UED regime was undertaken in 1986 through the introduction of modified value added tax (Modvat), which was based on the Report of the Jha Committee²⁷. This scheme provided a set-off for the taxes paid on inputs used in about a dozen articles. In 1987, the scheme was extended to cover some additional commodities.

The processes of reform in indirect taxes got strengthened in post 1991 when structural adjustment program was initiated to revive the Indian economy. To

²⁶ This section has been drawn liberally from Purohit 2009.

²⁷ Government of India 1978.

begin with, based on the recommendations of the Report of the Tax Reforms Committee (TRC), the Modvat was further extended to encompass a large number of commodities²⁸. The procedures of Modvat have been overhauled since then, converting the existing UEDs into Central VAT or CenVAT, which covers almost all items, except high-speed diesel (HSD), motor spirit (gasoline) and matchboxes. The Union Budget 2006-2007 converted the CenVAT into a two-rate duty structure of 16 percent and 8 percent. However, now the rate of CenVAT has been reduced to 14%.

CenVAT allows instant credit for all the taxes paid on inputs in the form of UEDs (i.e. Modvat/CenVAT) or additional duties of excise (ADE). Input credit is also given for additional duty of customs, which is known as countervailing duty (CVD)²⁹ and is collected at the time of the imports. For capital goods, however, only 50 percent of the duty can be claimed as input credit in a financial year; the remaining credit can be claimed in the next financial year, provided the goods are still in use (except for spares and components).

A manufacturer producing only tax-exempt final products is not allowed to claim this credit. However, it is permissible for a manufacturer who produces both dutiable and exempted final products in the same factory³⁰.

Along with CenVAT, the Union government also levies the additional excise duty in lieu of the sales tax³¹; additional duty of excise on textiles and textile articles; and cess on specified commodities.

3.2.2. Service Tax

The Constitution was amended to include service tax in the Union List by inserting item 92(C) into the Seventh Schedule. This enables the Union to assign this tax to the states, solely or concurrently, whenever it so desires. It is to be noted that the services' sector contributes the largest share in GDP. Since 1994-95, when it was introduced under residuary entry in the Union List, the number of services has increased over the years and the leviable rate of service tax was also revised (Table 3.7). Initially, only three services were taxed, viz. general insurance, stock broking and telephone. The coverage of the tax was gradually expanded and presently service tax is levied on 106 services. At present, the standard tax rate is 10% with effect from February 24th, 2008. The service tax is now integrated with CenVAT.

²⁸ Government of India 1993

²⁹ This has been discussed in the Annex 1 and subsequent part of this section.

³⁰ This is subject to certain conditions, viz. maintenance of separate records in respect of inputs used to manufacture exempted products or payment of 8 percent of the total price (excluding taxes) of the exempted final products or in the case of a few specified items, on reversal of the credit availed.

³¹ Additional excise duty in lieu of the sales tax has been levied since 1956 on tobacco, textiles and sugar under a tax rental arrangement between the Union and the States. According to this arrangement, the Union government was levying the additional excise duty on these items and the States refrained from levying sales tax on them. The net proceeds of this duty have been distributed among the States based on consumption. With the efforts of the country to move towards VAT, the proceeds of this tax is now included in the divisible pool, and the states have also been allowed to levy VAT on these items.

Table 3.7 Service Tax: Growing Revenue Source

Year	Number of services	Number of assesses	Tax rate (per cent)	Revenue (Rs. billion)	Growth (per cent)
2002-03	52	232048	5	41.2	24.8
2003-04	60	403856	8	78.9	91.4
2004-05	75	740267	10	142.0	80
2005-06	84	806585	10	230.6	62.4
2006-07	99	918746	12	376.0	63.1
2007-08 ^P	106	NA	12	513.0	36.4
2008-09(RE)		NA	12*	650.0	26.7

P provisional

Source: Government of India 2009

3.2.3. State-VAT

While the Union government at a central level levies a Cen-VAT on all manufactured goods and a service tax (integrated with CenVAT), all the states levy a state-VAT on goods sold within the state. Previously, different models of the single-point, double-point and multi-point sales tax were adopted in different States. However, the models adopted initially were replaced by a first-point sale tax and gradually, almost all the States switched over to this system. In addition to first-point sale tax, the States also imposed some other levies related to sale tax. These were in the form of additional sale tax, turnover tax or surcharge on sale tax. Considerable variations existed in these levies among the States.

The first-point sale tax, as well as the other supplementary taxes, suffered from many weaknesses such as cascading and uncontrolled incidence, multiplicity of rates, vertical integration of firms, non-neutrality and lack of efficiency in the tax system. Given these deficiencies in the prevailing structure of a sale tax, efforts were made to replace it with a system of sub-national VATs. Under a sale tax regime, all the States gave huge concessions and sales tax incentives to attract new industries. The Government of India took the initiative to design an acceptable structure for VAT. This was accomplished by a study report titled Reform of Domestic Trade Taxes in India in 1994³².

Finally, the following consensus emerged. The report was discussed in a number of forums involving Chief Ministers and Finance Ministers of all states so that differences among states could be resolved. Finally, the following consensus emerged:

- The number of rates prevailing under the sales tax would be reduced to a four-rate structure;
- The number of exemptions under the sales tax would be curtailed considerably;

³² NIPFP 1994

- No new tax exemptions (known as incentives) would be given to the industries and the existing incentives converted into deferment; and
- VAT should replace the existing sales tax system.

It was felt that prior to introduction of VAT, some preparations were essential. The States had attempted to rationalize their existing sale tax system by adopting two major reforms. The first reform related to the adoption of a four-rate structure (i.e. zero, 4, 8 and 12.5 percent) in the existing sale tax. These rates were in addition to two special rates of 1 percent and 20 percent for a few specified items. The recommended rates were flooring rates – the States had the freedom to adopt a higher rate on any of the commodities from the list. This had checked the rate war and diversion of trade among the states. However, when the states started implementing the four-rate categories many of them found it difficult to impose it on some commodities. Either the classification faced some problem or there were administrative difficulties in implementing the floor rates. Hence, a few changes were made in the items falling under the exempt list and in other categories.

The second reform pertains to the abolition of incentives related to sale tax as all the states granted various incentives to new industries in the form of exemption from tax on the purchase of inputs/sale of finished goods as well as sales tax loans and/or tax deferral. Various studies and committee reports³³ have already argued against such incentives and pointed out that these incentives take the form of tax competition (war) or harmful tax practices in a federation.

The VAT was finally introduced in most of the states from 1st April 2005. Haryana (a northern state) was the first State to introduce VAT on April 1st, 2003. Eventually, the rest of the states implemented the same. As of now, all the states have a system of VAT, known as state-VAT. The coverage of tax includes a sale of all goods, except diesel, petrol (gasoline), aviation turbine fuel, natural gas and liquor. It has two basic rate categories of 4% and 12.5% (standard rate) with some tax-exempt items and two special categories: 1% on gold, silver, and ornaments and 20% on petroleum products.

3.2.4. Harmonization of Interstate Tax

As stated earlier, taxation of inter-state transactions is in of the Union List of the Constitution. However, while the authority to levy the tax remains under the jurisdiction of the Union Government, section 9 of the Central Sales Tax Act entrusts the task of administering the tax to the states. The states are also allowed to retain this revenue. In effect, the tax has been assigned to the states. Thus, the tax is administered, collected and retained by the exporting state, based on 'origin'.

Although the CST serves the purpose of regulating the flow of interstate movement of goods, it's not compatible with the concept of a unified market in a federal country like India. It is contrary to inter-jurisdictional equity, causes cascading, discriminates against the consuming states, hinders the formation of common Indian market and causes the levy of tax on exports to other states. Also, its procedural requirement causes corruption in the tax administration.

³³ Government of India 1998 and 1999.

Keeping in view the above stated weaknesses and the demands of the open and liberalized economy, it was felt that an 'origin base' tax hampers the inter-state trade and puts Indian industry and business at a considerable disadvantage in comparison to producers abroad, whose products are now being imported on an increasing scale. In addition, India has made a commitment in the SAARC that all the SAARC countries should move towards free trade. Hence, breaking barriers across states has become necessary. There is an increasing realization that the tax on inter state sale is distortion and breaks the chain of transactions in the Indian common market. Thus, it becomes imperative to abolish CST. It has, however, now been decided to phase CST out by 1% point every year, to as to reduce it to zero by March 31, 2010³⁴. In doing so, the Union Government has announced some compensatory measures for the States, which are as follows:

Table 3.8. Contribution of each Major Tax of States in GDP (% of GDP)

Year	1990-91	1995-96	2000-01	2005-06	(RE) 2006-07	(BE) 2007-08
Tax revenue#	5.29	5.37	6.00	7.60	8.09	8.20
Direct taxes^	0.22	0.19	0.37	0.87	0.96	1.00
a) Land revenue	0.11	0.11	0.07	0.08	0.07	0.07
b) Corporation income tax (CIT)	n.a.	n.a.	0.21	0.72	0.81	0.85
c) Wealth tax	n.a.	n.a.	neg.	neg.	0.01	0.01
d) Others*	0.11	0.07	0.10	0.07	0.07	0.07
Indirect Taxes^	5.08	5.19	5.63	6.73	7.13	7.20
a) State excise duties	0.84	0.72	0.75	0.73	0.74	0.70
b) General sales tax	2.89	2.84	3.25	3.70	3.75	3.83
c) Stamp & registration fees	0.37	0.50	0.44	0.72	0.77	0.81
d) Tax on vehicles	0.27	0.31	0.31	0.34	0.34	0.33
e) Custom duties	n.a.	n.a.	0.23	0.51	0.55	0.57
f) Service tax	n.a.	n.a.	0.01	0.19	0.25	0.28
g) Others**	0.71	0.82	0.63	0.54	0.74	0.69
Non-tax revenue	0.97	1.50	0.96	0.96	0.99	0.90

Source: Indian Public Finance Statistics, and CMIE.

Note: * Hotel receipts tax, Share of estate duty, Agriculture tax, and others

** Motor spirit sales tax, Tax on goods & passengers, Tax & duty on electricity, Entertainment tax, Tax on purchase of sugarcane (incl. cess on sugarcane), and Others

^ Direct and Indirect taxes minus share of income tax, share of union excise duties

Gross tax revenue minus share of income tax, share of union excise duties

neg.: negligible

- Withdrawal of the benefit of concessional CST rate on inter-state sale to government departments.
- Enabling states to levy VAT on tobacco @ 12.5%.
- Transferring to the States the revenue from 33 services currently subject to Service Tax and assigning 44 new services to them (as and when taxed).
- Filling any gap through budgetary support in the years of transition in case the measures indicated at (a), (b) and (c) do not fully cover the revenue loss.

³⁴ It has already been reduced to 2 percent from April 1st, 2008.

3.2.5. A Way towards GST

After successful implementation of state-level Value Added Tax (VAT) in all the states, further reforms involving the introduction of a goods and service tax (GST) are under their way. It is planned that GST will be introduced with effect from the 1st April 2010.

The basic objective for transition to GST is to have an efficient, effective and taxpayer friendly system of taxation of goods and services in line with the best international practices. Also, there is a need for preserving the sovereign powers of the union and state governments in taxation matters. Furthermore, the need is to propose a model that is easy to implement and is also acceptable to all the stakeholders. However, there are significant structural, procedural and administrative issues involved in designing an effective GST model in a federal system, given the main objective of having a unified market.

Keeping this in view, the Empowered Committee of State Finance Ministers (EC) constituted a Joint Working Group to give recommendations regarding a detailed framework to be adopted for GST. The Joint Working Group recommended a dual GST as it felt that a single harmonized GST is impossible, given the prevailing Center-state relationship as well as the federal character of the economy. The Working Group has recommended that the GST should subsume all the indirect taxes on supply of goods or services, as given below:

- Central Excise duties and the Additional Excise duties levied on pan masala, petroleum and tobacco products, and those levied under Additional Duties of Excise (Goods of Special importance) Act, 1957;
- Additional customs duty in the nature of countervailing duties; special Additional Duty;
- Special Additional Duty and other domestic taxes imposed on imports to achieve a level playing field between domestic and imported goods (which are currently classified under a customs duty);
- Cesses levied by the Union, viz. cess on manufactured biris; rubber; tea; coffee; and cess on unmanufactured tobacco; and
- Surcharges levied by the Union, viz. national calamity contingent duty, education cess, special additional duty of excise on motor spirit and high speed diesel.

It is to be noted that some of the above cess and surcharges are earmarked for predetermined purposes, viz. education or uplift of the workers engaged in a particular industry, development of technology, etc. These do not currently form part of the CenVAT chain and are levied under independent Acts, legislated by different Ministries.

These levies, therefore, could be out of the purview of GST. The Working Group further recommends that the state-GST should include in its purview purchase tax, state excise duty³⁵, entertainment tax, luxury tax, octroi, entry tax in lieu of octroi, taxes on lottery, betting and gambling, tax on consumption or sale of electricity.

³⁵ However, the idea of subjugation of state excise duty requires reconsideration. Firstly, it is an important source of revenue in many of

With the above central and state taxes being subsumed under GST, the proposed GST will have two components – Central GST (levied by the Center) and State GST (levied by the states). The rates of these two components will be prescribed separately keeping in view the revenue considerations, total tax burden and the acceptability of the tax.

The effective rate of state-VAT is currently 12.5 percent, while the rate of CenVAT is 16 percent. Hence, the combined tax rate is 28.5 percent. This has to be reduced to approximately 15 to 20 percent, given the rate structure around the world.

3.3. Customs Duty

In the initial years after independence, India's dependence on custom duty was lower compared to other low income countries that had significant reliance on taxes on international trade due to India's efforts to restrict imports³⁶ to save scarce foreign exchange.

Duties of customs are levied on goods imported or exported from India at the rate specified under the customs' Tariff Act, 1975, and administered by Central Board of Excise and Customs in the Ministry of Finance, Government of India. For the purpose of exercising proper surveillance over imports and exports, the Union government has the power to notify the ports and airports for the unloading of the imported goods and loading of the exported goods, the places for clearance of goods imported or to be exported, the routes by which above goods may pass by land or inland water into or out of India and the ports.

Rates of customs duty for goods imported from countries with whom India has entered into free trade agreements such as Thailand, Sri Lanka, BIMSTEC, south Asian countries and MERCOSUR countries are different (Annex 4 lists the countries under various groups evolved in recent time).

Custom duty consists of basic tariff, which is the protecting element, and the Additional Duty of Customs (AD), that is a counterpart of excise duties paid by Indian manufacturers on a like product produced in India. If a like product is not manufactured or produced in India, the excise duty that would be leviable on that product had it been manufactured or produced in India is the duty payable. If the product is leviable at different rates, the highest rate among those rates is the rate applicable. Such duty is leviable on the value of goods plus basic custom duty payable. It is also called as countervailing duty (CVD). In addition, Special Additional duty (SAD) is levied to counter taxes imposed on raw materials, components and other inputs similar to those used in the production of such goods³⁷. The basic duty is levied under the Customs Act. The rate varies for different items. The Additional Duty (Countervailing Duty) is levied under section 3 (1) of the Custom Tariff Act and is equal to excise duty levied.

the states. Secondly, it falls in the category of sumptuary excises. Also, the Indian Constitution assigns a special role to the states for prohibition through this tax.

³⁶ Chelliah, 1986.

³⁷ Furthermore, states may also impose taxes on the sale of imported goods after they move from the port or out of the State in which it is located.

Special Additional Duty (SAD) is levied under section 3(3) of the Customs Act. It can be charged on all goods by the Union government. Further, in order to safeguard the interest of domestic manufacturers, as per the situation, the Union government may also impose anti-dumping duty, protective duty and duty on bounty fed articles (see Annex 1). On the other hand, Export Duty is levied on export of goods on few articles such as skins and leather. The main objective of this duty is to restrict exports of certain goods.

Thus, the import duty is collected essentially under four sub heads, i.e., basic custom duty, Additional Duty of Custom (AD) or Countervailing Duty (CVD), Special Additional Duty (SAD) and Education Cess. One may notice wide variations between a nominal basic tariff and the effective rate. Some commodities like, alcohol and automobiles have a basic rate higher than the peak rate. Please see Annex 2 for the list of these commodities.

Until the Long Term Fiscal Policy introduced in 1985, the custom tariff rates were very high with complex structure in highly protected and inward looking economy. Attempts were made to rationalize the structure. As a result, the tariff rates have been declining since 1991. The peak rate has come down from 150 percent in 1991-92 to 40 percent in 1997-98, 30 percent in 2002-03, 25 percent in 2003-04, 15 percent in 2005-06 and finally 10 percent in 2007-08. The peak rate of basic customs duty on non agricultural products, which was 20 percent in 2003-04 was successively reduced in subsequent budgets to reach a level of 10%. In 2007-08, the Budget for 2008-09, however, did not carry this forward as the appreciation of the rupee vis-à-vis US\$ by 9.8 percent in 2007³⁸ itself resulted in lower protection to domestic industry³⁸.

With the decline of the average tariff rate over the last two decades, the reliance on custom duty in the tax structure has also declined (tables 3.2 to 3.8). Though, average tariff remains among the highest in the world. All finance ministers in the past had made the statements to bring India's custom tariff to the level of ASEAN (Annex 4).

Even if India's peak rate is brought down to 10%, it still has to reach the tariff levels of East Asia. On the other hand, most ASEAN rates have been reduced further under the ASEAN free trade (AFTA) agreement. At the same time, the neighboring countries in South Asia, such as Bangladesh, Nepal and Sri Lanka, also have lower average tariffs than that of India. This creates another problem of import diversion and smuggling as India has some kind of free trade agreement with some of its neighbours. Hence, it is profitable to import items first in the neighboring countries and export them from there to India. As described above, there have been continuous changes in the customs' tariff structure since 1991. It is close to the ASEAN level. Still, India's tariff structure is one of the highest in the world. Simultaneously, the custom duty structure is complex as it contains 1150 pages with 4000 devoted to its examples. Secondly, nonagricultural tariff needs to be reviewed concerning its classification and administration.

³⁸ Government of India 2009, p. 40.

3.3.1. High Tariff³⁹

One can argue to impose a high tax on certain consumer goods to discourage their consumption. This does not, however, translate easily into an argument for imposing higher import tariffs on the “undesirable goods.” Thus, for example, if the Government of India wants to discourage the consumption of alcohol, the best way to do this is to have higher excise taxes and an equivalent additional custom duty. This is indeed what the Government already does. Imposition of a high import tariff, on the other hand, cuts off competition from better quality alcohol, and removes the incentive for upgrading the quality. It also provides an incentive for smuggling.

Items such as automobiles, air conditioners, furniture and fixtures are used both by consumers and producers. Higher tariff protection in such cases will have adverse effects on the effective protection provided to all industries because they constitute a part of the costing structure. There is one argument in the trade literature, i.e., the “Infant Industry Argument” that has often been used to justify “protection” of both “pure” consumer goods and dual use items such as cars. Even in this case, however, the (so called) first best or efficient solution is a direct subsidy to producers. Direct subsidies have the additional benefit of transparency in that the cost of protection of each protected item is measured by the known subsidy.

It is very important to note that an industry cannot be an “infant” forever; it may be an “infant” for five years or at the outer limit 10 years. Twenty and thirty year old industries cannot be called “infant industries.” As time passes by, the efficiency of the industry diminishes due to complacency. Thus, any such protection must be limited in both scope and time. Moreover, the OECD countries, researchers dealing with infant industry argument have not been able to identify specific industries that would clearly and unambiguously benefit from such temporary protection. It has proven even more difficult to demonstrate that such specific interventions would be welfare improving.

3.3.2. Low Tariff

There can also be a valid social argument for lower taxes on certain (pure) consumer goods like life saving drugs, medical devices and equipment and knowledge related goods. As in the previous case this is really an argument for reducing domestic consumption taxes like CENVAT and Sales tax along with the corresponding additional duty or special additional duty (SAD). Reduction of domestic taxes and SAD is an economically efficient way of ‘subsidising’ the use of these items.

Once this stand is taken, the classical, efficient, economic solution is quite clear⁴⁰. A direct subsidy on consumption is the best means of facilitating consumption. When there are a large number of suppliers (producers or traders) the administrative costs of such subsidy can be very high⁴¹. Therefore under exceptional situation of high administrative

³⁹ Drawn from Virmani 2002.

⁴⁰ Prof. Bhagwati and Srinivasan demonstrated in a number of papers that the best way of dealing with domestic distortions is through domestic policy changes to offset them, not through trade distorting measures. Please see for example Srinivasan and Vani 2009.

⁴¹ As demonstrated in the case of food and petroleum subsidies.

cost and high standard tariff rate it may be socially desirable to reduce the customs tariff below this rate. The reduction should be considered an interim measure till the standard rate is brought down to a reasonable level.

3.3.3. Single Rate

The phased reduction in the “peak” rate of basic customs duty is going on. Simultaneously, exemption and anomalies in the structure should be removed except for those arising from international agreements and higher temporary protection of agricultural raw materials. A single uniform rate of basic (protective) customs duty on all imports has many attractive features, including the following:

- a) “It ensures that the nominal protection for all imports is the same, thus, eliminating all classification problems and disputes, resulting in substantial savings in administrative and legal costs.
- b) It makes it much easier to administer the duty free import regime for exporters. As a single rate applies to all imports, only a total value of imports needs to be specified.
- c) Most imports can, in principle, be on self-declaration basis and customs staff can focus their time and energy on checking smuggling (through mis-declaration of quantity or concealment of an item) and chronic misstatements of price.
- d) If the uniform rate is reasonably low, the incentive for smuggling will be minimized and make the administrative problem of checking it manageable.
- e) With a single, uniform, nominal duty, the effective protection rate is also identically equal to this rate. The rate of effective protection is, therefore, neutral and equal to all value added by domestic producers. This will increase the efficiency and competitiveness of the entire economy.
- f) Uniform effective protection on all producers’ goods is more equitable in that it removes the discrimination against other producers. Higher protection for one set of producers inevitably results in lower protection for some other producer.
- g) In the case of final finished consumer goods, there is much greater economic justification for a single uniform basic customs duty equal to that on producer goods (with AD/SAD – domestic taxes on consumer goods) then, there is for a single uniform rate VAT or CENVAT (applying equally to domestically produce and imported goods).
- h) A low uniform rate duty will have the additional benefit of reducing India’s weighted average tariff rates below those prevailing in neighboring countries. Economic interests of India will then become much more closely aligned with neighbors. Indian industry and agriculture will have much less to fear from special free trade arrangements with India’s neighbors than is the case today.
- i) A low uniform duty that is close to the average for ASEAN countries will enhance India’s case for closer economic integration with ASEAN. India can then take the lead in the formation of an Asian Common Market, instead of being treated as a highly protected economy.

- j) Such a regime will eliminate the continuous lobbying that now takes place and the special benefits to large industry and powerful interest groups and losses to the small and unorganized that inevitably result from such lobbying⁴².

3.4. Taxation and E-commerce

In general, e-commerce, which refers to conducting trade via the Internet, has a much larger scope than just conducting merchandise transactions electronically. It not only includes all forms of trade in goods, but also encompasses services such as banking, insurance and trading in shares.

E-commerce creates diverse functions and revenue streams. Also, it reduces costs of transactions significantly. It is believed that procurement costs will be reduced by 90 percent through buying online. It is estimated, for example, that online banking costs one rupee against Rs. 27 by cash machine and Rs. 114 by bank teller⁴³.

In view of the reduced costs and increased efficiency of e-commerce as compared to the traditional system of trade and commerce, growth of e-commerce is likely to be highest in India among the Asian nations. Estimates show that it will grow at the rate of 246 percent in India against 84 percent in Australia, 110 percent in Hong Kong, 145 percent in South Korea and 243 percent in China⁴⁴. With the industry and trade rapidly picking up computer culture, its full potential will be reality in India in the near future. The opening up of the economy and globalization will stimulate its use and have a deep effect on the system of tax governance in the country.

With a view to encourage e-commerce, most countries initially adopted the policy of exempting e-commerce from taxation. The 'infant industry' argument was the justification for such a policy. It is, however, important to note that the European Union has now started taxing e-commerce. The argument for taxation of e-commerce is based on the premise that such an exemption might induce other dealers/taxpayers to enter transactions that save them some tax. It is, therefore, important to evolve the principles that should govern taxation of e-commerce.

In this context, the Government of India constituted a high powered committee on Electronic Commerce and taxation on December 16th, 1999⁴⁵. The objective of the Committee was to examine the projected growth of E-Commerce business and whether it should be subject to tax, etc. Some of the observations made by the committee are as follows.

- No reliable data exists as to the estimate of E-Commerce business either in India or elsewhere.
- There has to be uniformity in the taxation of traditional commerce and E-Commerce and to that extent, there is no case for exemption of E-Commerce from Direct Tax.

⁴² Virmani 2002, p.13-14

⁴³ Purohit and Purohit 2006 Ibid.

⁴⁴ Virmani 2002, p.13-14

⁴⁵ Government of India 2001b.

- There is no issue regarding domestic E-Commerce taxation, except for the need to avoid evasion because of the lack of records. In respect to cross border E-Commerce, however, there is a need to examine the incidence of tax and a mechanism to levy and collect the same.

Significantly, the Committee has come to the view that applying the existing principles and rules to E-Commerce is impractical and the concept of "PE" (permanent place of establishment) adopted by few countries and backed up by article 5 of the OECD model tax convention should be rejected.

The Committee feels that the "Base Erosion" approach in the form of a low "Withholding tax" for any payment to a foreign enterprise with the option of being offset by tax on net income by the receiver in his country is a workable option. It has been recommended that Central Board of Direct Taxes (CBDT) should examine this option and the implementation mechanism.

The approach of the Committee is considered pragmatic. The CBDT is suggested by experts to initiate necessary dialogue with the International community to generate consensus on the approach and establish a suitable mechanism. In the interregnum, status quo can continue⁴⁶. Presently, the revenue from E-commerce is too low to hold the attention of tax authorities.

4. Economic Development

4.1. Macroeconomic Developments

In the late eighties, Prime Minister Economic Advisory Council headed by Sukhmoy Chakravarty drew pointed attention of the Government of India towards two fundamental imbalances, i.e. trade imbalance and the fiscal imbalance. The growth rate was also low.

Though, India had slow growth during 1950-80, what is called "Hindu growth rate" of 3.5 percent for GDP.⁴⁷ In the early nineties, the Narasimha Rao government of which Manmohan Singh was the finance minister initiated the structural adjustment program.

The program comprised 10 broad policy prescriptions (Table 4.1) including fiscal discipline and tax reform. Under the program, as mentioned in the previous section, many measures were taken to reform major taxes with an underlying direction towards broader bases with moderate rates and fewer exemptions. A conducive environment for trade and industry was created. As a result, the growth rate picked up.

⁴⁶ The debate on international taxation of e-commerce is inconclusive. Azam 2007 argues that the debate is oriented and ignores cyber space law and this separation is unjustified and harmful to the development of e-commerce taxation law.

⁴⁷ Even growth rate of 3.5 per cent of GDP was more than four times higher than the growth rate of 0.8 per cent per year estimated for the last five decades of British rule (Sivasubramoniam 2000).

Table 4.1. The Washington Consensus

1 Fiscal discipline
2 Reordering public expenditure in favor of education, health and economic infrastructure
3 Tax reform (towards broader bases with moderate rates)
4 Financial liberalization
5 Competitive exchange rate
6 Trade liberalization
7 Liberalisation of foreign direct investment
8 Privatisation (of public enterprises)
9 Deregulation (of barriers to entry and exit)
10 Property rights

Source: Williamson (1990)

The optimism about Indian economic development continued during the period. As a corollary, the economy grew between 1960-79, 1980-91, 1992-2002 and 2002-05 periods at an annual average rate of 3.5, 5.5, 6.0 and 8.1 percent respectively. The pace of economic growth, which is regarded as the primary indicator of macroeconomic health, was unprecedented over 2003-04 to 2007-08 with an average growth rate of 8.8 percent per year. The growth decelerated in 2008-09 to 6.7 percent. This represented a decline of 2.1 percent from the average growth rate of 8.8 percent in the previous five years. However, during the preceding five-year period, from 1998-99 to 2002-03, the average growth rate was only 5.5 percent due to several reasons, including political uncertainties of coalitional government and a high fiscal deficit due to large public pay increases.

Table 4.2. Growth of Real GDP (Percent per year)

	1992/93- 1996/97	1997/98- 2001/02	2002/03- 2006/07	2002/ 03	2003/ 04	2004/ 05	2005/ 06	2006/ 07	2007/ 08
GDP(factor Cost)	6.6	5.5	7.8	3.8	8.5	7.5	9.4	9.6	9.0
Agriculture	4.8	2.5	2.5	-7.2	10.0	0.0	5.9	3.8	4.5
Industry	7.3	4.3	9.2	7.1	7.4	10.3	10.1	11.0	8.5
Services	7.3	7.9	9.3	7.5	8.5	9.1	10.3	11.1	10.8
Per capita GDP	4.4	3.5	6.1	2.3	6.9	5.8	7.7	8.1	7.5

Source: Acharya, 2008 (Basic Data -CSO).

Note: Agriculture comprise of agriculture proper, forestry & logging, and fishing. Industry includes mining & quarrying, manufacturing, electricity, gas & water supply, and construction. Services includes trade, hotel, transport & communication, finance, insurance, real estate and business services, and social & personal services

This includes the enhancement of total factor productivity (TFP)⁴⁸, buoyant international economic environment and an extraordinary growth of a modern service

⁴⁸ TFP may be defined as the ratio of output to a weighted combination of inputs. It reflects the efficiency with which factors of production are used, and is thus a key determinant of an economy's performance, especially its international competitiveness. One of the most important sources of TFP growth in the long run is technological progress.

sector, including communications, information technology and finance. The expansion of the service sector has been unprecedented. Today, its share in GDP is about 55 percent compared to one fifth share of the agriculture and one fourth shares of industry (table-4.3). Agriculture growth remains low during the period as the sector depends substantially on weather conditions. However, during 2005-08, its contribution to the GDP was noteworthy as it registered the annual growth rate between 4 to 6 percent, whereas the GDP growth rate hovers between 9 to 10 percent in the corresponding period. It is to be noted that despite low growth in agricultural it employs over half of India's labor force.

Table 4.3. Sectoral Composition of Growth

	Share in real GDP (%)		Contribution to GDP Growth (%)		
	Average of 1994-97	Average of 2004-07	1991/92 to 1996/97	1996/97 to 2001/02	2001/02 to 2007/08
Agriculture	28.2	19.4	21.1	11.5	7.0
Industry	26.4	26.5	29.0	20.2	29.3
Services	45.4	54.1	49.8	68.3	63.6
GDP (Factor Cost)	100.0	100.0	100.0	100.0	100.0

Source: same as table 4.2.

On the other hand, Table 4.4 shows the composition of GDP growth from the expenditure side. Share of aggregate investment expenditure in GDP is showing considerable rise, whereas government and private sector consumption grew from 1996-97 to 2001-02, but declined thereafter.

Table 4.4. Expenditure Composition of Growth

	Share in real GDP (%)		Contribution to GDP Growth (%)		
	Average of 1994-97	Average of 2004-07	1991/92 to 1996/97	1996/97 to 2001/02	2001/02 to 2007/08
Investment (GDCF)	23.9	32.6	29.2	20.4	57.3
Government Final Consumption	11.1	10.2	8.2	16.7	5.3
Private Final Consumption	65.7	59.6	54.3	60.2	47.9
Net Exports of Goods and Services (including Discrepancies)	-0.7	-2.4	8.4	2.7	-10.5
GDP (Factor Cost)	100.0	100.0	100.0	100.0	100.0

Source: same as table 4.2.

4.2. Total Factor Productivity

Many things contributed to the unprecedented economic growth that India witnessed in the last two decades. Total factor productivity (TFP)⁴⁹ is certainly an important element. India registered two percent increase in average annual output growth between pre reform period of 1978-93 and post reform period of 1993-04. Of this two percentage point increase, 1.2 points were attributable to improved TFP, which more than doubled from an average annual growth of 1.1% during 1978-93 and 2.3% during the period 1993-04 (Bosworth and Collins 2007). The rest of the rise was largely due to increased investment. Improved TFP contributed to roughly half of the increase in labor productivity, which almost doubled between the two periods; the rest of the increase was mainly due to higher investment. Improved TFP was also largely responsible for the substantial increase in the rate of growth of capital productivity.

Table 4.5. Total factor productivity in India, 1978-04 (Percent change per year)

	Overall		Agriculture		Industry		Services	
	1978-93	1993-04	1978-93	1993-04	1978-93	1993-04	1978-93	1993-04
Output	4.5	6.5	2.7	2.2	5.4	6.7	5.9	9.1
Employment	2.1	1.9	1.4	0.7	3.3	3.6	3.8	3.7
Capital	1.0	1.8	0.2	0.7	1.4	1.7	0.3	1.1
Land	-0.1	0.0	-0.1	-0.1	n.a.	n.a.	n.a.	n.a.
Education	0.3	0.4	0.2	0.3	0.4	0.3	0.4	0.4
TFP	1.1	2.3	1.0	0.5	0.3	1.1	1.4	3.9
Labour productivity	2.4	4.6	1.3	1.5	2.1	3.1	2.1	5.4
Capital productivity	1.8	2.4	1.7	0.5	1.4	2.2	3.5	5.5

n.a. Not applicable.

Source: Bosworth B. and Collins S. 2007 as presented in WTO, 2007

Growth in both output and TFP has been much faster in the services' sector than in industry (where performance has seemingly been hampered by, inter-alia, rigid labor laws and inadequate infrastructure). By contrast, growth in output and TFP in agriculture has slowed (possibly due to weather and other natural factors). It follows that the shifting of resources, especially labor from agriculture (where more than half of the labor force is employed) to the more productive industry and tertiary sectors would contribute to faster overall growth in output and TFP in the economy as a whole⁴⁹.

⁴⁹ WTO 2007

4.3. The Human Development Index

Since 1990, performance has been measured beyond income growth to a broader definition of well-being through the Human Development Index (HDI)⁵⁰. As per the UNDP's Global Human Development Report (HDR) 2007, the HDI for India improved from 0.577 in 2000 to 0.611 in 2004 and further to 0.619 in 2005. Although it has gone down to 0.609 in 2006, the relative ranking of India has not changed much. India is ranked at 132 among the countries with medium human development out of 179 countries of the world.

4.4. Infrastructure Development

Infrastructure is the crucial sector that plays the key role in the development process of India. For the purpose, special attention is paid to this sector by combining the efforts of public and private sectors. Hence, physical infrastructure, especially electric power, telecom, railways and roads and ports have been funded with adequate investment. Total investment in infrastructure has been estimated to be around 5% of GDP. It is viewed that the gross capital formation (GCF) in infrastructure should rise as a share of GDP from 5% in 2006-07 to 9% by the end of 2011-12 (Table 4.6).

Table 4.6. Gross Capital Formation in Infrastructure Based on Growth Targets (Top-down Estimates at 2006-07 price)

Year	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
GDP Market Price (Rs. billion)	41458.1	45189.3	49256.4	53689.4	58521.5	63788.4
Rate of growth of GDP (%)	9.0	9.0	9.0	9.0	9.0	9.0
GCF in infrastructure as % of GDP	5.0	5.8	6.5	7.3	8.0	9.0
GCF in infrastructure (Rs. billion)	2072.9	2598.4	3201.7	3892.5	4681.7	5741.0
GCF in infrastructure (US\$ billion)	51.8	65.0	80.0	97.3	117.0	143.5
Total GCF in Eleventh Plan	Rs 20115 billion or US\$ 502.88 billion					

Source: Eleventh Five Year Plan Report

A comparative picture of the sector-specific allocations in the two Plan periods is given in table 4.7. Compared with investment levels achieved in the Tenth Plan period, the expected infrastructure investment in the Eleventh Plan is 2.36 times the amount of US\$ 217.86 billion at constant 2006-07 price. The telecom, transportation (comprising ports and airports), and storage improves their share in the total investment in the Eleventh Plan as compared to their share in the Tenth Plan. Irrigation, electricity and the transportation sectors comprising roads and railways are expected to invest more than double the actual absolute investment in the Eleventh Plan, but would register some decline as a proportion in the overall pie. The need for investment in the electricity

⁵⁰ HDI provides a composite measure of three dimensions of human development: living a long and healthy life (measured by life expectancy), being educated (measured by adult literacy and enrolment at the primary, secondary and tertiary level) and having a decent standard of living (measured by purchasing power parity, PPP, income). The index is not in any sense a comprehensive measure of human development. It does not, for example, include important indicators such as gender or income inequality and more difficult to measure indicators like respect for human rights and political freedoms. It only provides a broader prism for viewing human progress and complex relationship between income and well-being.

Brazil, Russia, India and China (BRIC)

Tax system structures and the effects on development and foreign trade performance - lessons and solutions

sector is greater than what has been projected. However, a realistic assessment suggests that even the projections made so far would pose serious policy and implementation challenges. If these challenges can be overcome in time, actual investments could exceed these projections⁵¹.

4.5. Foreign Investment Flows

Until recently, international investors were not seeing India as an attractive investment destination due to a number of factors including sub optimal infrastructure, industry unfriendly tax policies, political instability, etc. In any case, India on its own had acquired restrictive attitude towards foreign investment. In the nineties as mentioned earlier, India began to open up its economy. As mentioned earlier, many measures were taken to reform the tax system at the level of Center and states. Foreign investment flows started to pick up in the 1990s and have gathered further momentum in the past few years. Foreign investment comprising foreign direct investment (FDI) and portfolio investment on a net basis was US\$ 14.8 billion in 2006-07 and US\$ 45.0 billion in 2007-08 (204.7 percent growth), before slowing down to US\$ 4.0 billion during 2008-09 (April-December). As a proportion of total capital flows, net foreign investment stood at 41.6 percent in 2007-08 (32.6 percent in 2006-07). However, its share declined to 26.4 percent during 2008-09 (April-December) on account of FII outflows pursuant to the global financial crisis⁵².

Table 4.8. Source wise Distribution of India's Inward FDI Stock 1991-2009 (Rs. Million)

Country	(1991-1999 Aug-Dec)		(Jan.2000 to March 2009)	
	Value	Per cent	Value	Per cent
Mauritius	124659	21.611	1619734	40.906
U.S.A.	83542	14.483	285606	7.213
Netherlands	21743	3.770	159290	4.023
Japan	29694	5.148	115690	2.922
U.K.	22279	3.862	229621	5.799
Germany	23511	4.076	95335	2.408
France	9638	1.671	55203	1.394
Singapore	12393	2.149	338565	8.550
Korea(South)	20921	3.627	20405	0.515
Switzerland	7951	1.378	38838	0.981
Others*	131253	22.755	740237	18.695
Brazil	23	0.004	69	0.002
China	19	0.003	507	0.013
Russia	1749	0.303	19345	0.489
BRC**	1791	0.310	19920	0.503
Grand Total	576821	100.000	3959647	100.000

* Includes other countries, advance of inflow, stock swapped, and nri-rbi schemes.

** BRC refers to Brazil, China, and Russia.

Source: Ministry of Commerce & Industry, Department of Industrial Policy & Promotion
http://siadipp.nic.in/publicat/pub_mn.htm

⁵¹ Eleventh Five Year Plan Report Inclusive growth 11th_vol I, p 256

⁵² Government of India 2009.

Out of both foreign investments, FDI is perceived to be the most coveted type of capital flow for an emerging economy as it brings modern technology and enhances production capabilities. During 2005-06 to 2008-09, FDI flows assumed greater significance.

High inflows indicate India as an attractive investment destination as a result of its liberalized investment climate, stable and sound economic and political base, opportunities for economic growth, while capital investment abroad reflects the growing global competitiveness of the Indian corporate sector. The two-way flow of FDI, therefore, means that while the world is taking note of India's market potential, Indian companies are also constantly looking for synergistic acquisitions abroad.

With the reforms in the policies, better infrastructure and vibrant financial sector, FDI inflows into India have accelerated since 2006-07. On a gross basis, FDI inflows into India increased from US\$ 8.9 billion in 2005-06 to US\$ 22.8 billion in 2006-07 and further to US\$ 34.4 billion in 2007-08. In the fiscal year 2008-09 (April-December), gross FDI into India was US\$ 27.5 billion. FDI inflows are spread across a range of economic activities like financial services, including banking, manufacturing, information technology services and construction.

FDI has grown significantly on a net basis. The year-to-year growth in FDI (net) was 153.6 percent in 2006-07 and 100.2 percent during 2007-08. Even as FDI flows into India grew substantially, a simultaneous pickup in outward investment moderated the overall net inflows. Outward investment by India increased from less than US\$ 2.4 billion during 2003-04 and 2004-05 to US\$ 15.8 billion in 2006-07 and US\$ 21.3 billion in 2007-08.

During fiscal 2008-09 (April-December), FDI into India (net) remained buoyant at US\$ 27.4 billion (US\$ 20.0 billion in April-December 2007) reflecting relatively better investment climate in India and the continuing liberalization measures to attract FDI. Outward FDI (net) continued to remain high at US\$ 12.0 billion during April-December 2008 even in the current economic situation, though it was marginally lower than its previous year's level of US\$ 13.1 billion. Due to large inward flows, the net FDI (inward minus outward FDI) was higher at US\$ 15.4 billion in April- December 2008, as compared with US\$ 6.9 billion in April-December 2007. As per the UNCTAD 2008, India achieved a growth of 85.1 percent in FDI inflows, which was the highest globally⁵³. The total flows increased from US\$ 25.1 billion in 2007 to US\$ 46.5 billion in 2008. This is despite 14.5 percent decline in global FDI inflows from US\$ 1,940.9 billion in 2007 to US\$ 1,658.5 billion in 2008. India also ranked 9th in global FDI inflows in 2008⁵⁴ followed by Brazil. On the other hand, China is ranked 5th followed by Russia (Table 4.9). It is considered that robust economic growth, an improved investment environment and opening up of critical sectors like telecommunications, civil aviation, refineries, construction, etc., facilitated FDI inflows into India.

⁵³ In terms of UNCTAD Survey 2008-10, China is the most preferred investment destination, followed by India, the United States, the Russian federation and Brazil. Similarly, AT Kearney's 2007 FDI Confidence Index shows China, India and USA as the most preferred locations in that order. For long-term prospects, JBIC survey of Japanese manufacturing Transnational Corporations (TNCs) showed India replacing China as the most promising country for business operations of Japanese TNCs. (Government of India 2009)

⁵⁴ Government of India 2009.

Table 4.9. Foreign Direct Investment in Top 11 Countries (US\$ billion)

Rank in 2008	Countries	2007	2008*	Growth rate (%)
1	USA	232.8	320.9	37.8
2	France	158.0	126.1	-20.2
3	UK	196.4	96.8	-50.7
4	Belgium	70.0	94.2	34.6
5	China	83.5	92.4	10.6
6	Russia	52.5	70.3	34.0
7	Spain	68.8	65.5	-4.8
8	Hong Kong China	59.9	63.0	5.2
9	India	25.1	46.5	85.1
10	Brazil	34.6	45.1	30.3
11	Sweden	22.1	40.4	83.1
	World	1940.9	1658.5	-14.5

* Preliminary Estimates

Source: Government of India 2009

*Portfolio investment*⁵⁵: Net portfolio inflows into India were US\$ 7.0 billion in 2006-07 and US\$ 29.4 billion in 2007-08. Portfolio investment by FIIs, however, witnessed large net outflows of US\$ 12.4 billion during April-December 2008 (as against net inflows of US\$ 24.5 billion in the corresponding period of 2007) due to large scale sale of equities by FIIs in the Indian stock market. FII outflows for the year 2008-09 amounted to US\$ 15 billion vis-à-vis net inflow of US\$ 20.3 billion during the year 2007-08⁵⁶.

4.6. Double Taxation Avoidance

The Double Taxation Avoidance Agreements (DTAA) came into being when a resident of one jurisdiction has income source in another jurisdiction. In such cases, the normal rule says that the jurisdiction in which the concerned person is a resident has the right to tax his income. However, the source jurisdiction also has the authority to tax the income. Such taxation by the latter may be subject to a maximum permissible rate. A Double Taxation Avoidance Agreement may effectively provide for avoidance of tax or for relief against double taxation by providing grant of credit by the jurisdiction of residence of the tax paid in the source jurisdiction. Tax Avoidance Agreements may be confined to a particular type of income. The first concrete step for relieving against double taxation, in so far as India is concerned, was taken in 1939 with the enforcement of the Income tax – Double Taxation Relief – Indian States Rules. Since then, India has comprehensive DTAA with 79 countries. Under Income Tax Act 1961 of India, there are two provisions – section 90 and section 91 – which provide specific relief to tax payers to save them from

⁵⁵ Portfolio investment includes foreign institutional investors (FIIs) investment, issue of global depository receipts (GDRs)/American depository receipts (ADRs) and offshore funds.

⁵⁶ Government of India 2009

DTAA. Section 90 is for tax payers who have paid the tax to a country with which India has signed DTAA, while Section 91 provides relief to tax payers who have paid tax to a country with which India has not signed DTAA. Thus, India gives relief to both kinds of tax payers⁵⁷. Annex 5 contains DTAA treaties that India had signed before.

A large number of Foreign Institutional Investors who trade on the Indian stock markets operate from Mauritius. According to the tax treaty between India and Mauritius, Capital Gains arising from the sale of shares are taxable in the country of residence of the shareholder and not in the country of residence of the Company whose shares have been sold. Therefore, a company resident in Mauritius selling shares of an Indian company will not pay tax in India. Since there is no capital gains tax in Mauritius, the gain will escape tax altogether.

5. Conclusions

Wilson and Puroshothaman 2003, from Goldman Sachs, invented the acronym BRIC to describe Brazilian, Russian, Indian and Chinese economies. It is now widely used and "*BRIC funds are an important part of the emerging-markets universe*"⁵⁸. The Goldman Sachs predicted that the four economies would comprise more than 10 percent of the global output by the end of the decade; the four economies reached 15 percent in 2008. Leaders of the four BRIC nations participated in the first BRIC Summit in Yekaterinburg, Russia on June 16, 2009. All of them agreed for strengthening cooperation and coordination among themselves to promote dialogue in an open and transparent way. Many feel that this group can play a vital role in international politics as the world's largest growing economies are getting together on the same platform and discussing a common concern. During the current economic meltdown, it is also felt that the emerging countries such as BRIC are expected to perform better than the global average.

India as an emerging country is no exception to this trend. For the last few years, India's economic performance has been impressive averaging over 7% between 2001-02 and 2006-07. It posted a robust average growth rate of more than 9% during 2005-07. Rapid economic growth has translated into an improvement in social indicators, including a decline in infant mortality, a reduction in the percentage of the population living below the poverty line and improvements in literacy, sanitation and access to clean water.

This impressive performance is largely due to unilateral trade and structural reforms, which have been continued during the period. Growth has been led by the services' sector, where liberalization has been most rapid. Manufacturing has also performed well, although further growth may be impeded by infrastructure and other constraints.

In contrast, agricultural growth continues to be slow and erratic and dependent on the weather, causing considerable distress, especially among small and marginal farmers⁵⁹.

⁵⁷ en.wikipedia.org/wiki/Double_taxation

⁵⁸ Economist, April 21, 2008.

⁵⁹ WTO, 2007

The Government is aiming to sustain growth in the longer run. Recognizing the importance of continuing its economic reform and especially its trade aspects, India has pushed ahead with further reductions in the tariff: There has also been simplification of the tariff, although it remains complex. The Government is targeting higher export growth in order to sustain India's high levels of economic growth and has put in place a set of schemes to reduce the anti-export bias of the trade regime for exporters.

Despite a gradual increase in total tax revenue India's tax to GDP ratio is relatively low and seemingly insufficient to meet its developmental needs. Further public spending on infrastructure and social services is constrained by the Fiscal Responsibility and Budget Management (FRBM) Act, 2003, which requires India to reduce its fiscal and revenue deficits and to eliminate the revenue deficit by 31st March 2009. However, the government deviated from these targets in the election year. At present, there is no credible signal from the government for moving towards fiscal consolidation. The Central government uses the excuse of the global recession to justify the high public expenditure that is being called fiscal stimulus.

India has a Parliamentary system. The Lower House is elected directly and sits for five years, while the Council of States includes representatives elected by the legislative assemblies of the states. Executive power is vested in the President, who appoints the Prime Minister and other members of the Cabinet. The Cabinet must be composed of Members of Parliament. India's legal system is based on written law. The judiciary is headed by the Supreme Court, which has jurisdiction over all disputes between the Central Government and states or between the states. The Supreme Court is also the court of final appeal for cases heard by the High Court in each state, and by district and session courts at the local level. The legal system is burdened by insufficient resources and procedural delays, resulting in a large and apparently growing backlog of cases before the high courts and the lower courts. Measures are being taken to address the backlog of cases.

India is a federal country. Powers of taxation have been divided between the Center and the states. The local governments, both rural and urban, are also part of the federal ensemble in India, although their actual powers are decided by the respective state government.

As per the constitutional arrangements, the Central government has a buoyant source of revenue, i.e. corporate income tax, personal income tax, central excise/CenVAT and customs, whereas State government relies on sales tax/state VAT. In the Indian Constitution, most responsibilities have been decentralized to the sub national government. The provision is largely consistent with provisions mentioned in the theoretical literature of public finance. However, the mismatch between the revenue power and expenditure responsibility gives rise to vertical imbalance that is corrected through the mechanism of intergovernmental fiscal transfers from Center to states. The money flows through various institutional arrangements. Finance Commission, a constitutional body, and Planning Commission, created through an order of the Executive, are the two most important institutions in this regard. Finance Commission constituted

in every five years recommends the formula for vertical and horizontal distribution of the taxes that the Central government collects. These transfers are generally for revenue expenditure, e.g. salary to government employees, expenditure on operation and maintenance. The Planning Commission transfers the plan fund. In addition, it funds also flows through various central schemes. In short, intergovernmental fiscal transfer mechanism in India is quite complicated and creates dissatisfactions at all levels across the states.

Before 1991, the tax system in India was archaic, irrational and complex. It interfered with the free play of market forces and competition, caused economic distortions and entailed a high cost of compliance and administration. In the earlier socialist pattern of development, the extraordinary high rate of income taxes was compelling tax payers to evade taxes. The manner in which the commodity taxes were levied and administered caused:

- "Loss of output growth and welfare;
- Inefficiency and high cost in industry and trade;
- Impediments to the free flow of trade with the country and growth of the common market that the Indian Union offers;
- Inter-jurisdictional conflicts;
- Handicap for exports; and
- High costs of compliance and enforcement"⁶⁰

Measures have been taken to simplify the tax structure, especially for indirect taxes, resulting in a substantial increase in a revenue collection. Tax reforms have also been pursued to meet the fiscal deficit and an introduction of a value-added tax regime covering both the governments, i.e. the Center and the states and an increase in the number of services subject to a service tax. The introduction of the VAT by almost all states has paved the way for goods and service tax. Excise duty (CENVAT), which is a tax on manufacturing, but has the elements of a value-added tax, provides around 20% of total tax revenue. The CENVAT remains the largest source of indirect tax revenue. In the longer run, further streamlining of India's various indirect taxes is planned so that the VAT, the CENVAT and the service tax will be replaced by a broad-based goods and service tax. As a corollary, complex custom duty structure would also be simplified.

As mentioned in section II, the custom duty is an important source of Union government tax revenue and contributes about 17 percent in total tax revenue and its ratio to GDP is 2 percent. It is also the main trade instrument of India. The government has taken a number of measures to reform trade related matters. Applied MFN tariffs, especially for non-agricultural products, have continued to fall steadily. The overall trend in tariff rates continues to be downward. The "peak rate" is reduced to 10%. Despite gradual reform over the years, the tariff remains complex: tariff changes are announced throughout the year and with numerous exemptions, a number of, which are based on industrial use. India also offers tariff preferences under its regional trade agreements. However, apart from the agreement with Sri Lanka and preferences to LDC members of SAFTA, the preferences do not appear to be significant.

⁶⁰ NIPFP, 1994

India is a major user of anti-dumping measures, although the numbers of investigations and measures in force have been on decline. Steps are being taken to align national standards increasingly with international norms; currently, some 73% of national standards, for which corresponding international standards exist, are aligned with these international norms. In general, national standards are subject to review every five years to ensure that they keep up with international trends. India is not a member of the WTO Agreement on government procurement. Its procurement policies have undergone reform, especially at the Central government level, although preferences continue to be extended to certain items from the small-scale industry and from state-owned enterprises. While import barriers have been falling, India's export regime continues to be complex. Export prohibitions and restrictions are large in numbers. However, in order to reduce the anti-export bias inherent in India's import and indirect tax regime, a number of duty remission and exemption schemes are in place to facilitate exports. While a number of these schemes are open to all exporters who use imported inputs, several schemes are targeted at sectors such as electronics (hardware and software), agricultural products and services. Export processing zones, export-oriented units that are now called special economic zones (SEZs) also offer tax holidays to investors.

According to Ministry of Finance estimates, revenue forgone from such schemes is in the range of five to eight hundred billion rupees in recent years. India also provides export assistance through export insurance and financing schemes by the Export-Import Bank of India.

In addition, internal reforms have concentrated on increasing competition and efficiency in the economy. Industrial policy reforms have concentrated on simplifying and reducing restrictions. The number of items reserved for production only by the small-scale sector has declined from 799 in 2001 to 326 in May, 2006.

The high growth in India stems from the structural adjustment program initiated in 1991 of which tax reform and trade liberalization are the integral components. In order to sustain the high growth, India needs to give pace to its existing reforms and initiate further reforms to eradicate, inter alia, poverty and infant mortality. As the world expected in the beginning of this decade, India's future looks bright despite uncertainties that Indian democracy has learnt to manage over time. Mahatma Gandhi said, "Democracy is the art and science of mobilizing the entire physical, economic and spiritual resources of various sections of the people in the service of the common good at all⁶¹. This is precisely what we will have to do.

6. References

- ACHARYA, Shankar 2005, "Thirty Years of Tax Reform in India", *Economic and Political Weekly*, Volume 40, N°. 20, May 14.
- _____. 2006, "Economic Growth: Some Reflections", *Economic and Political Weekly*, November 4.
- _____. 2009, *India's Macroeconomic Performance and Policies since 2000*, ICRIER Working Paper N°. 225, October

⁶¹ Quoted in Government of India, 2009, Budget, 2009-10, Speech of Minister of Finance, July 6.

- Administrative Reforms Commission 1968, Report of the Study Team on Centre-State Relationship, v. I, New Delhi, Government of India
- AHMAD, Ehtisham and Nicholas Stern 1991, *Theory and Practice of Tax Reform in Developing Countries*, Cambridge, Cambridge University Press
- AKYUZ, Yilmaz, 2005, *The WTO Negotiations on Industrial Tariffs, What Is At Stake for Developing Countries*, Third World Network, Penang.
- ALOK, V N 2006, "Rural Local Government: Organization and Finance", in Anwar Shah (ed) *Local Governance in Developing Countries*, Washington, DC., The World Bank
- _____. 2009, "Share of Local Governments in the Union Divisible Pool: An Option before the 13th Finance Commission", *The Indian Journal of Public Administration*, Vol. LV, Jan-Mar, N^o. 1.
- ANDERSON, Robert D. 2006, "Meeting the challenges of good governance, the complementary roles of trade liberalization and competition rules in addressing anti-competitive barriers and practices in national procurement markets". Paper prepared for an International Conference on Public Procurement, Global Revolution III, Session on Combating Collusion in Public Procurement University of Nottingham, 1-20 June.
- AZAM, Rifat, E-commerce 2007, *Taxation and Cyberspace Law: The Integrative Adaptation Model*, Virginia Journal of Law and Technology, vol 12, N^o. 5, Summer.
- BAGCHI, Amaresh, 1998, Tax Assignment in Indian Federation: A Critique, in Isher Judge Ahluwalia and IMD Little (eds.) *India's Economic Reforms and Development. Essays for Manmohan Singh*, OUP, Delhi.
- BAGCHI, A. and Pulin Nayak 1994, "A Survey of Public Finance and the Planning Process, The Indian Experience", in Bagchi,-Amaresh and Stern,-Nicholas, (eds). *Tax Policy and Planning in Developing Countries*. Delhi, Oxford University Press.
- BHATTACHARJEA, Aditya 2006, "Amending India's Competition Act," *Economic and Political Weekly*, 14 October.
- BIRD, Richard, 1989, "The Administrative Dimension of Tax Reform in Developing Countries" in Gills, Malcolm (ed) *The Theory and Practice of Tax Reform in Developing Countries*, Duke University Press London , 1989, pp. 315-345.
- BOSWORTH B. and Collins S. 2007, "Accounting for Growth: Comparing China and India", *Economics of Developing Countries Papers*
- CASANEGRA de Jantscher, Milka 1990, "Administering VAT" in Gillis,-Malcolm; Shoup,-Carl-S.; Sicut,-Gerardo-P.,(eds). *Value Added Taxation in Developing Countries*, A World Bank Symposium, Washington, D.C., The World Bank.
- CHADHA, R. 2000. 'GATS and Developing countries, A Case Study of India', Paper commissioned by the World Bank.
- _____. 2002. *Globalization of Services, India's Opportunities and Constraints*. New Delhi, Oxford University Press.
- _____. 2005. 'India's Stake in the WTO Services Negotiations', in Bibek Debroy and Mahammed Saqib (eds), *WTO at Ten, Looking Back to Look Beyond*, Vol II, Issues at Stake, pp. 21-74. Konark Publishers, New Delhi.
- CHAKRAVARTHY, S. 2005, "India", in Douglas H. Brooks and Simon J. Evenett, (eds), *Competition Policy and Development in Asia*, New York, Asian Development Bank and Palgrave MacMillan.
- CHANG, Ha Joon 2005 'Developing Countries Need to Wake Up to the Realities of the NAMA Negotiations', *TWN Briefing Paper* 26.
- CHATURVEDI, Sachin and S K Mohanty 2008, *The WTO and Trade in Electronically Delivered Software: Emerging Challenges and Policy Options – An Indian Perspective*, *Journal of World Trade* 42 (5) October, Wolters Kluwer.
- CHELLIAH, Raja J.1986 "Change in the Tax Structure: A Case Study of India", Paper Presented at the 42nd Congress of International Institute of Public Finance, Athens, Greece.
- CMIE, I-Cube service, Centre for Monitoring the India Economy Pvt Ltd.
- DAS-GUPTA, Arindam and Dilip Mookherjee 1997, *Design and Enforcement of Personal Income Tax in India*, in Sudipto Mundle (ed.) *Public Finance, Policy Issues for India*, Themes in Economics, Oxford in India Readings, Oxford University Press
- DAS-GUPTA, Arindam 2002 "Central Tax and Administration Reform in the 1990s, An assessment" in M. Govinda Rao (ed.) *Development, Poverty and Fiscal Policy, Decentralisation of Institutions*, Oxford India Paperbacks, Oxford University Press, New Delhi.

- _____. 2004, "The Income Tax Compliance Cost of Corporations in India, 2000-2001" NIPFP Working Paper N^o. 8, March
- _____. 2004a, "The Compliance Cost of the Personal Income Tax in India, 2000-2001, Preliminary Estimates" NIPFP Working Paper N^o. 9, March 2004.
- Government of India 1953, Report of the Taxation Enquiry Commission, Ministry of Finance, New Delhi, India.
- _____. 1956. Indian Tax Reform, Ministry of Finance, New Delhi.
- _____. 1971. Direct Taxes Enquiry Committee, Final Report, Ministry of Finance, New Delhi, India.
- _____. 1978. Report of the Indirect Taxation Enquiry Committee, Ministry of Finance, New Delhi.
- _____. 1991. Tax Reforms Committee, Interim Report, Ministry of Finance, New Delhi,
- _____. 1993. Report of the Tax Reforms Committee, Vol. II and III, Ministry of Finance, New Delhi
- _____. 1998. Report of the Finance Ministers Committee to Chart a Time Path for the Introduction of VAT, August
- _____. 1999. Report of the Committee of Finance Secretaries for Identification of Backward Areas, November
- _____. 2001. Report of the Advisory Group on Tax Policy and Tax Administration for the Tenth Plan, Planning Commission, May.
- _____. 2001a. Report of the Expert Group on Taxation of Services, Ministry of Finance, New Delhi,
- _____. 2001b. Report of the High Powered Committee on Electronic Commerce and Taxation, Central Board of Direct Taxes, New Delhi
- _____. 2002. Report of the Taskforce on Indirect Taxes, Ministry of Finance, New Delhi, India, December.
- _____. 2002a. Report of the Taskforce on Indirect Tax, 24 December, New Delhi.
- _____. 2003. Report of the Task Force on Implementation of the Fiscal Responsibility and Budget Management Act, Ministry of Finance, New Delhi,
- _____. 2004. Report of the Twelfth Finance Commission, New Delhi
- _____. 2005. Ministry of Law and Justice, The Constitution of India,
- _____. 2006. Export Promotion of Consultancy and Management Services from India, Consultancy Development Centre, March, Ministry of Commerce and Industry.
- _____. 2006. Foreign Trade Policy 2004-2009, Handbook of Procedures, v. 1, Chapter II, April, Ministry of Commerce and Industry New Delhi.
- _____. 2006. Foreign Trade Policy, 1 September 2004-31 March 2009, Ministry of Commerce and Industry, Viewed at, [http http, //dgft.delhi.nic.in](http://dgft.delhi.nic.in).
- _____. 2006. Department of Justice, <http://mha.nic.in/justi.htm>
- _____. 2009., Economic Survey 2008-09, Ministry of Finance, New Delhi.
- _____. 2009a. Union Budget 2009-10, Ministry of Finance New Delhi.
- HAUSMANN, Ricardo, Dani Rodrik and Andres Velasco 2005, 'Growth Diagnostics', John F Kennedy School of Government, Harvard University, Cambridge, Massachusetts, March
- HAUSMANN, Ricardo, Lant Pritchett and Dani Rodrik 2005, 'Growth Accelerations', Journal of Economic Growth, 10(4), December, pp 303-29.
- KHOR, Martin and Goh Chien Yen 2006, The WTO Negotiations on Non-Agricultural Market Access, A Development Perspective, Third World Network, Penang.
- KUMAR, S. 2005. Trade in Service: Advantage India, New Delhi, Bookwell.
- MCLURE Jr., Charles 1983, Tax Assignment in Federal Countries, Canberra, Australian National University.
- MOHANTY, S K 2008, Rise of BICS and the World Economy Implications of India's Recent Expansion on Developing Countries, New Delhi, RIS, (RIS Discussion Paper 138).
- MOHANTY, S.K. and Sachin Chaturvedi (2009) Emerging Trade and Investment, Linkages between India and Africa, Challenges and Prospects (processed).
- MUKHERJEE, A. and N. Patel, 2005. FDI in Retail Sector, India, New Delhi, Academic Foundation.
- MUKHOPADHYAY, S. 2006, "Which way for indirect taxes", Economic and Political Weekly, April.
- MUSGRAVE, Richard 1983 "Who should Tax Where and What' in Mclure (ed.)
- NIPFP 1994, Reform of Domestic Trade taxes in India, Issues and Options, National Institute of Public Finance and Policy, New Delhi
- NIPFP 1996, Report of the Committee of State Finance Ministers on Stamp Duty Reform, NIPFP.

- PODDAR, Tushar 2004, 'Domestic Competition Spurs Exports, The Indian Example', Working Paper N°. 04/173, IMF, Washington, DC.
- PODDAR, Tushar and Eva Yi 2007, 'India's Rising Growth Potential', Goldman Sachs Global Economic Paper N°. 152, January.
- POIRSON, H. 2006. "The Tax System in India, Could Reform Spur Growth?", IMF Working Paper WP/06/93, April, Washington, D.C.
- PUROHIT, Mahesh C. 2001, Sales Tax and Value Added Tax in India, Delhi, Gayatri Publications.
- _____. 2009. A Road Map for GST, Foundation for Public Economics and Policy Research (Working Paper).
- PUROHIT, Mahesh C. and Vishu Kanta Purohit 2006, E-commerce and Economic Development, EPEPR, Delhi, Gayatri Publication
- PURUSHOTHAMAN, Roopa 2004, 'India, Realizing BRICs Potential', Goldman Sachs Global Economic Paper N°. 109.
- RAO, M.G. 2005, "Tax System Reform in India, Achievements and Challenges Ahead". International Symposium on Tax Policy and Reform in Asian Countries, 1-2 July, Tokyo.
- RBI 2008, Annual Policy Statement for the Year 2008-09, Mumbai.
- RODRIC, Dani and Arvind Subramanian, 2004. 'Why India can Grow at 7 percent a Year or More, Projections and Reflections', Working Paper N°. 04/118, IMF, Washington, DC.
- RODRIC, Dani. 'Goodbye Washington Consensus, Hello Washington Confusion?', Journal of Economic Literature.
- SHAH, Anwar 1994, The Reform of Intergovernmental Fiscal Relations in Developing and Emerging Market Economies, Washington, DC, World Bank Research Series.
- SHIVA Rao, B 1968, The Framing of India's Constitution, New Delhi, Indian Institute of Public Administration
- SIVASUBRAMONIAN, S 2000, The National Income of India in the Twentieth Century, Oxford University Press, New Delhi.
- SRINIVASAN, T.N. and Vani Archana 2009, India in Global and Regional Trade: Determinants of Aggregates and Bilateral Trade Flows and Firms' Decision to Export, ICRIER Working Paper N°. 232, February.
- SOLOW, Robert M 1956, 'A Contribution to the Theory of Economic Growth', Quarterly Journal of Economics 70, pp 65-94.
- SURY, M.M. 2008, Centre State Financial Relations in India, 1870 to 2010, New Delhi, Indian Tax Foundation.
- TANEJA, Nisha, 2004. Trade Facilitation in the WTO, Implications for India, ICRTER, UNCTAD, 2001 'Best Practices for Enhancing the Competitiveness of Developing Countries'. Report of the Expert Meeting on Electronic Commerce and International Transport Services.
- Transparency International 2005, Corruption Perceptions Index. Viewed at, http://www.transparency.org/policy_research/surveys_indices/cpi/2005
- _____. 2005a. India Corruption Study, 2005. Viewed at, <http://www.tiindia.in/data/files/India%20Corruption%20Study-2005.pdf>. and viewed at: http://www.opacityindex.com/opacity_index.pdf
- _____. 2009. Global Corruption Report, viewed at, <http://www.transparency.org/publication> [23 July 2009].
- UNCTAD 2008. "Assessing the Impact of the Current Financial and Economic Crisis on Global FDI Flows"
- Virmani, Arvind, B.N. Goldar, C. Veeramani and Vipul Bhat 2004, "Impact of tariff reforms on Indian industry, Assessment based on a mutli-sector econometric model", ICRIER Working Paper N°. 135.
- VIRMANI, Arvind. 2002. Towards a Competitive Economy: VAT and Customs Duty Reform (working paper no. 4/2002-PC), Planning Commission.
- WILSON, Dominic, ROOPA Purushothaman. 2003, 'Dreaming with BRICs, The Path to 2050', Goldman Sachs Global Economic Paper N°. 99.
- WILLIAMSON, John. 1990. 'What Washing Tax Means by Policy Reform' in Williamson (ed.) Latin American Adjustment: How Much Has Happended? Institute for International Economics, Washington, DC.
- WTO 2002, Trade Policy Review, India, Geneva.
- _____. 2005. "International Trade in Air Transport, Recent Developments and Policy Issues", World Trade Report, Geneva.
- _____. 2007. Trade Policy Review, India, Geneva

7. ANNEXES

Annex 1 – Legal Structure of Major Taxes in India⁶²

Tax on Corporate Income

Companies residents in India are taxed on their worldwide income arising from all sources in accordance with the provisions of the Income Tax Act. Non-resident corporations are essentially taxed on the income earned from a business connection in India or from other Indian sources. A corporation is deemed to be resident in India if it is incorporated in India or if its control and management are situated entirely in India. A company has been defined as a juristic person having an independent and a separate legal entity from its shareholders. Income of the company is computed and assessed separately in the hands of the company. However, the income of the company, which is distributed to its shareholders as dividend, is assessed in their individual hands. Such distribution of income is not treated as expenditure in the hands of the company. The income so distributed is an appropriation of the profits of the company. Domestic corporations are subject to tax at a rate of 33.9% (including education surcharge and education cess). Foreign corporations have a tax rate of 42.33% (including education surcharge and education cess). Corporations are subject to wealth tax at the rate of 1%, if the net wealth exceeds Rs. 1.5 million (US\$ 31,000 approx.).

Domestic corporations have to pay dividend distribution tax at the rate of 12.5%. It is proposed to be increased to 15% in the Union Budget presented on July 6, 2009. However, such dividends received are exempt in the hands of the recipients. Corporations have to pay for Minimum Alternative Tax at 10% (plus surcharge and education cess) of book profit as tax if the tax payable as per regular tax provisions is less than 10% of its book profits. It is proposed to be increased to 15% in the Union Budget presented on July 6th, 2009.

Capital Gains Tax⁶³

A capital gain is income derived from the sale of an investment. A capital investment can be a home, a farm, a ranch, a family business, or a work of art, for instance. In most years, slightly less than half of taxable capital gains is realized on the sale of corporate stock. The capital gain is the difference between the money received from selling the asset and the price paid for it. Tax is payable on capital gains on sale of assets. Long-term Capital Gains

⁶² Drawn from http://finance.indiamart.com/taxation/corporate_tax/index.html

⁶³ "Capital gains" tax is a misnomer. It is more appropriate to call it the "capital formation" tax. It is a tax penalty imposed on productivity, investment, and capital accumulation. The capital gains tax is different from almost all other forms of taxation in that it is a voluntary tax. Since the tax is paid only when an asset is sold, taxpayers can legally avoid payment by holding on to their assets—a phenomenon known as the "lock-in effect." There is unfairness imbedded in the current tax treatment of capital gains. One is that capital gains are not indexed for inflation: the seller pays tax not only on the real gain in purchasing power, but also on the illusory gain attributable to inflation. The inflation penalty is one reason that, historically, capital gains have been taxed at lower rates than ordinary income. In fact, most capital gains were not gains of real purchasing power at all, but simply represented the maintenance of principal in an inflationary economy. Another unfairness of the tax is that individuals are permitted to deduct only a portion of the capital losses that they incur, whereas they must pay taxes on all of the gains. That introduces an unfriendly bias in the tax code against risk taking. When taxpayers undertake risky investments, the government taxes fully on gain that they realize from positive return of the investment. But the government allows only partial tax deduction if the venture goes sour and results in a loss.

Tax is charged if capital assets are held for more than three years and. In the case of shares, securities listed on a recognized stock exchange in India, units of specified mutual funds, the period for holding is one year.

Long-term capital gains are taxed at a basic rate of 20%. However, long-term capital gain from a sale of equity shares or units of mutual funds is exempt from tax. Short-term capital gains are taxed at the normal corporate income tax rates. Short-term capital gains arising on the transfer of equity shares or units of mutual funds are taxed at a rate of 10%. Long-term and short-term capital losses are allowed to be carried forward for eight consecutive years.

Long-term capital losses may be offsetting against taxable long-term capital gains and short-term capital losses may be offset against both long term and short-term taxable capital gains.

Personal Income Tax

Personal income tax is levied by Union Government and is administered by Central Board of Direct Taxes under Ministry of Finance in accordance with the provisions of the Income Tax Act. The rates for personal income tax after the revision in the Union budget 2009-10 are as follows:

Taxable Income Slab (Rs)	Rate (%)
Upto 1,60,000	Nil
Upto 1,90,000 (for woman)	Nil
Upto 2,40,000 (for senior citizen)	Nil
1,60,000 – 3,00,000	10
3,00,000 – 5,00,000	20
5,00,000 upwards	30

Withholding Tax

The Union government, under Section 90 of the Income Tax Act, has been authorized to enter Double Tax Avoidance Agreements (tax treaties) with other countries. The object of such agreements are to evolve an equitable basis for the allocation of the right to tax different types of income between the 'source' and 'resident' states, ensuring in that process tax neutrality in transactions between residents and non-residents. Domestic corporations are granted credit on foreign tax paid by them, while calculating tax liability in India.

A non-resident, under the scheme of income taxation, becomes liable to tax in India in respect to income arising here by virtue of its being the country of source and then again, in his own country in respect to the same income by virtue of the inclusion of such income in the 'total world income' which is the tax base in the country of residence. Tax incidence, therefore, becomes an important factor influencing the non-residents in deciding about the location of their investment, services, technology, etc.

Tax treaties serve the purpose of providing protection to tax payers against double taxation and thus preventing the discouragement which taxation may provide in the free flow of international trade, international investment and international transfer of

technology. These treaties also aim at preventing discrimination between the tax payers in the international field and providing a reasonable element of legal and fiscal certainty within a legal framework. In addition, such treaties contain provisions for mutual exchange of information and for reducing litigation by providing for mutual assistance procedure.

India has signed Double Taxation Avoidance Agreement with BRC at a different point of time – Brazil in 1994-95, Russia in 2000-01 and China in 1996-97 (Annex 5).

Current rates for withholding tax for payment to non-residents are:

- Interest 20%;
- Dividends paid by domestic company Nil;
- Royalties 10%;
- Technical Services 10%;
- Any other services;
- Individuals: 30% of the income; and
- Companies: 40% of the net income.

The above rates are general and are applicable in respect of countries with which India does not have a Double Taxation Avoidance Agreement.

Tax Incentives

Government of India provides tax incentives for:

- Corporate profit;
- Accelerated depreciation allowance;
- Deductibility of certain expenses subject to certain conditions.

These tax incentives are subject to specified conditions, available for new investment in:

- Infrastructure;
- Power distribution;
- Certain telecom services;
- Undertakings developing or operating industrial parks or special economic zones;
- Production or refining of mineral oil;
- Companies carrying on R&D;
- Developing housing projects,
- Undertakings in certain hill states;
- Handling of food grains;
- Food processing;
- Rural hospitals, etc; and
- Excise Duty/CENVAT.

Central excise revenue is the single largest contributor to gross revenue for the Government of India. Section 3 of the Central Excises and Salt Act, 1944, provides that there shall be levied and collected in such a manner as may be prescribed duties of excise on all excisable goods other than salt, which are produced or manufactured in India at the rates set forth in the schedule to the Central Excise Tariff Act, 1985. It is, therefore, clear that as soon as the goods in question are produced or manufactured, they will be liable to payment of excise duty. However, for convenience, duty is collected at the time of removal

of the goods. While Section 3 of the Central Excises and salt Act, 1944 lays down the taxable event, Rules 9 and 49 of the Central excise Rules, 1944 provides for the collection of duty.

Manufacture of goods in India attracts Excise Duty under the Central Excise Act 1944 and the Central Excise Tariff Act 1985. The term manufacture means bringing into existence a new article having a distinct name, character, use and marketability including packing, labeling, etc.

Most of the products attract excise duties at the rate of 16%. Some products also attract special excise duty/and an additional duty of excise at the rate of 8% above the 16% excise duty. Two percent education cess is also applicable on the aggregate of the duties of excise. Excise duty is levied on a ad valorem basis or based on the maximum retail price in some cases.

Service Tax

Service tax is levied at the rate of 10% (plus 2% education cess) on certain identified taxable services provided in India by specified service providers. Service tax on taxable services rendered in India is exempt, if payment for such services is received in convertible foreign exchange in India, and the same is not repatriated outside India. The Cenvat Credit Rules allow a service provider to avail and utilize the credit of additional duty of customs/excise duty for payment of service tax. Credit is also provided on payment of service tax on input services for the discharge of output service tax liability.

Customs Duty

Duties of customs are levied on goods imported or exported from India at the rate specified under the customs' Tariff Act, 1975, and administered by Central Board of Excise and Customs in the Ministry of Finance, Government of India. The rate varies for different items. The Additional Duty (Countervailing Duty) is levied under section 3 (1) of the Custom Tariff Act and is equal to excise duty levied. Special Additional Duty is levied under section 3(3) of the Customs Act. One may notice a wide variation between a nominal basic tariff and the effective rate. Some commodities like alcohol and automobiles have a basic rate higher than the peak rate (Please see Annex 2). The other details and analysis of the custom duties are given in the text.

Anti-dumping Duty: In order to capture Indian markets, when foreign sellers abroad export goods into India at the price below the price applicable in their domestic markets, the practice known as dumping is considered detriment of Indian industry. In order to prevent dumping, the Union government may levy additional duty equal to the margin of dumping on such articles if the goods have been sold at less than a normal value. Pending determination of margin of dumping, such duty may be provisionally imposed. After the exact rate of dumping duty is finally determined, the Union government may vary the provisional rate of dumping duty. Dumping duty can be imposed even when goods are imported indirectly or after changing the condition of goods. There are, however, certain restrictions on imposing dumping duties in case of countries which are signatories to the GATT or on countries given "Most Favored Nation Status" under the agreement. Dumping duty can be levied on imports

on such countries only if the Union government proves that import of such goods in India at such low prices cause material injury to Indian industry.

Protective Duty: If the Tariff Commission set up by law recommends that in order to protect the interests of Indian industry, the Union government may levy protective antidumping duties at the rate recommended on specified goods. The notification for levy of such duties must be introduced in the Parliament in the next session by way of a bill or in the same session if Parliament is in session. If the bill does not pass within six months of introduction in Parliament, the notification ceases to have a force but the action already undertaken under the notification remains valid. Such duty will be payable up to the date specified in the notification. Protective duty may be canceled or changed by notification. Such notification must also be placed before Parliament for approval as above.

Duty on Bounty Fed Articles: In case foreign country subsidizes its exporters for exporting goods to India, the Union government may charge additional import duty equal to the amount of such subsidies or bounty. If the amount of subsidies or bounty cannot be clearly determined immediately, additional duty may be collected on a provisional basis and after final determination, the difference may be collected or refunded, as the case may be.

Sales Tax/ State VAT

Sales tax is levied on the sale of movable goods. Most of the Indian States have replaced Sales tax with a new Value Added Tax (VAT) from April 01, 2005. VAT is imposed on goods only and not on services, and it has replaced the sales tax. There are four slabs of VAT:

- 0% for essential commodities;
- 1% on bullion and precious stones;
- 4% on industrial inputs and capital goods and items of mass consumption;
- All other items 12.5%; and

Petroleum products, tobacco, liquor, etc., attract higher VAT rates that vary from State to State. A Central Sales Tax at the rate of 4% is also levied on inter-State sales and is being phased out.

In addition, State levies other taxes, like Stamp duty on transfer of assets, agriculture income tax on income from plantations and Luxury tax levied on specified goods.

Taxes Levied by Rural and Urban Local Governments

The Annex Table 3 shows that a variety of taxes have been devolved to different levels of rural local governments (panchayats). The similar case is there for the urban local governments (municipalities). The relative importance of these taxes varies from state to state. The intermediate and district panchayats are endowed with powers to collect very few taxes, whereas village panchayats are given substantial taxing powers. In a number of cases, under the tax rental arrangement, the village panchayats collect taxes and pass them on to the higher level of panchayats. Property tax, cess on land revenue, surcharge on additional stamp duty, tolls, tax on professions, tax on advertisements, non-motor

vehicle tax, octroi, user charges and the like contribute the maximum to the small kitty of own-source revenue, which contributes only 6 to 7 percent of the total expenditure of panchayats. In most states, the property tax contributes the maximum revenue to the local governments both panchayats and municipalities. However, this tax remains inelastic because of inefficient administration in its collection. Its assessment is based on the annual rental value of taxation and its associated evil: under a declaration of rentals. However, some progressive states have reformed the tax structure and use the unit area method in determining the tax base.

Annex 2

Items with above "Peak" Basic Customs Duty Rates

Chap.	Description of Goods
N°.	Agriculture & Allied
2.	Poultry meat (Chicken leg)
4.	Other Milk powder (0402.10, 0401.21)
8.	Coconuts (0801.11, 0801.19)
8.	Areca nuts, others (0802.90)
8.	Dried grapes (0806.20)
8.	Apples (0808.10)
9.	Coffee (09.01)
9.	Tea (09.02)
9.	Pepper, cloves, cardamom (09.04, 09.06, 0908.30)
10.	Rice in the husk (paddy) & husked (brown) rice (10.0630.40)
10.	Semi-milled or wholly milled rice and broken rice (10.0630/40)
10.	Wheat, maize/corn, spelt, sorghum, millet (10.01/05/07/0820)
12.	Copra (12.03)
15.	Soya bean oil, crude or refined (15.07)
15.	Rapeseed/colza/mustard oil (crude or refined: 15.14)
15.	Palm/groundnut/sunflower/safflower/coconut/other oils: crude
15.	Palm/groundnut/sunflower/safflower/coconut/other oils: refined
16.	Sausages/meat prods of meat offal/blood (16.01), other prepared meat/offal/blood of fowls of species Gallus domesticus (16.0232)
17.	Sugar (17.01)
22.	Beer, grape must, wine, vermouth, other fermented beverages (22.03-06)
22.	Un-denatured ethyl alcohol (2207.10)
22.	Whiskies, rum, gin, vodka, liqueurs & cordials, etc. (22.08)
33.	Alcoholic preparations used to manufacture beverages (3302.10)
40.	Natural raw rubber latex (4001.01)
	Automobiles
87.	Motor cars and two wheelers, used (87.03, 87.11)
87.	Complete (CBUs of) Motor cars and two wheelers, new (87.03, 87.11)
	Other
98.	Baggage articles, other than on transfer of residence, above Rs. 12,000 (98.03)

Annex 3

India's commitments under various trade agreements until 2009

Agreement	Trade in goods	Trade in services	Other areas
SAFTA	Non-LDC members, including India, are to reduce tariffs to 20% within two years, followed by a reduction of 0-5% in five years (six years for Sri Lanka) and three years for imports from LDC members. India has a negative list of 744 imports from LDCs and 865 items from non-LDC members who are excluded from tariff reduction commitments. ^a The first tariff reductions came into effect on 1st July 2006.	n.a.	n.a.
Asia Pacific Trade Agreement (Bangkok Agreement)	Tariff preferences for 570 HS six-digit tariff lines and an additional 48 tariff bank line for LDC members with margin of preference ranging from 5% to 100%. Special concession on some items has also been extended to the LDCs.	n.a.	n.a.
BIMST-EC	Framework Agreement signed in February 2004 to form a free-trade area by 2012 with an additional five year given to the LDC members. Negotiations on trade in goods were to be completed by the end of 2005, but are yet to conclude. Negotiations on services and investment have commenced and must be concluded by 2007.	n.a.	n.a.
GSTP	Tariff concessions of 10%-50% on 53 tariff lines at the HS six-digit level. Tariff concessions of 50% apply to three tariff lines and are available only to Bangladesh, Benin, Guinea, Haiti, Mozambique, Sudan, and Tanzania.	n.a.	n.a.
Special preferential areas	Tariff preferences for certain imports from Mauritius, Seychelles, and Tonga.	n.a.	n.a.
Afghanistan	Tariff reductions on 38 HS six-digit tariff lines, with margins of preferences of 50% or 100% of the MFN tariff in force from 13 May 2003.	n.a.	n.a.
Nepal	Tariff exemptions for all goods subject to rules of origin. Imports of certain goods (vanaspati, copper products, acrylic yarn and zinc oxide) are subject to annual quotas.	n.a.	n.a.

Continues

Brazil, Russia, India and China (BRIC)

Tax system structures and the effects on development and foreign trade performance - lessons and solutions

Continued			
Singapore (CECA)	Zero duties as of 1 August 2005 for 506 HS eight digit products covered by the early harvest program. Phased reduction and elimination of duty by 1 April 2009 for 2,202 HS eight-digit products and phased reduction of duty by 50% by 1 April 2009 for 2,407 HS eight-digit products. Some 6,500 HS eight-digit products are excluded from duty reductions.	Business services, communication, construction, distribution, financial (banking), health, tourism, recreational and transport (maritime) services.	Investment, standards, SPS, intellectual property rights, science and technology, education and dispute settlement.
Sri Lanka	Zero duties as of 1 March 2000 for over 1,000 tariff lines and a 50% margin of preference for all other items except 429 items on a negative list. Tariff concessions on textiles are 25% below the MFN rate. Tariff quotas apply to tea and garments and vanaspati. Total quantum of import restricted to 250,000 tonnes per annum.	n.a.	n.a.
Thailand	Early harvest scheme for 82 products at the HS six-digit level; tariffs to be reduced in phases from 1 st September 2004 and to be eliminated by 1 st September 2006.	n.a.	n.a.
Bhutan	Non-tariff restrictions on the goods entry into respective territories. Trade will be transacted in Indian Rupees and Bhutanese Ngultrums.	n.a.	n.a.
MERCOSUR PTA	From 1st, June 2009 there is a tariff concession on 452 Indian products in MERCOSUR while a concession on MERCOSUR's 450 products in India.	n.a.	n.a.
PTA & Framework with Chile	Fixed tariff preferences ranging from 10% to 50% on 178 tariff lines at the eight digit level has been provided to Chile while Chile has offered tariff preferences on 296 tariff lines at the 8 digit level with margin of preference ranging from 10% to 100%.	Joint Study Group	It agrees to cooperate in customs, plant and animal health, technical standards and regulations, food safety, mutual recognition of sanitary and hytosanitary measures, including through equivalence agreements in accordance with relevant international criteria.
Framework Agreement with ASEAN	Progressive elimination of tariffs and non-tariff barriers in substantially all trade in goods, Common products on which the new ASEAN states agree to exchange tariff concessions are 105 while products on which India's accord concessions to the New ASEAN Member States are 111.	Progressive liberalization of trade in services with substantial sectoral coverage	Establishment of a liberal and competitive investment regime that facilitates and promotes investment within the India-ASEAN RTIA Regional Trade and Investment Area, Areas of Economic Corporation, Early Harvest Programme.

n.a. Not applicable.

a) India has offered Bangladesh market access for 8 million pieces of garments, of which 3 million using fabrics of Indian origin, three million using fabrics either of Indian or Bangladesh origin and two million unconditionally. This is part of India's sensitive list.

Source: Ministry of Commerce and Industry online information. <http://commerce.nic.in>

Brazil, Russia, India and China (BRIC)

Tax system structures and the effects on development and foreign trade performance - lessons and solutions

Annex 4

List of Regional Trade Agreements

SACU	GCC	BIMSTEC	Bangkok	EFTA
South Africa	Bahrain	Bangladesh	Bangladesh	Norway
Lesotho	Kuwait	Bhutan	Laos	Switzerland
Swaziland	Oman	Nepal	Republic of Korea	Iceland
Botswana	Qatar	Sri Lanka	Sri Lanka	Liechtenstein
Namibia	UAE	Thailand	Philippines	
		Myanmar	Thailand	
		India	India	

ASEAN	SAFTA	MERCOSUR	CIS	NAFTA	EU
Indonesia	India	Spain	Azerbaijan	Canada	Austria
Malaysia	Bangladesh	Portugal	Armenia	USA	Belgium
Philippines	Bhutan	Brazil	Belarus	Mexico	Bulgaria
Singapore	Nepal	Argentina	Georgia		Cyprus
Thailand	Sri Lanka	Uruguay	Kazakhstan		Czech
Brunei	Pakistan	Paraguay	Kyrgyz		Denmark
Vietnam	Maldives	Bolivia	Moldova		Estonia
Lao PDR		Chile	Russia		Finland
Myanmar		Columbia	Tajikistan		France
Cambodia		Ecuador	Uzbekistan		Germany
		Peru	Ukraine		Greece
					Hungry
					Ireland
					Italy
					Latvia
					Lithonia
					Luxembourg
					Malta
					Netherlands
					Poland
					Portugal
					Romania
					Slovakia
					Slovenia
					Spain
					Sweden
					United Kingdom

Annex 5

Double Taxation Agreement Treaties

S.No.	Name of the Country	Effective from Assessment Year	
1	Australia	1993-94	
2	Austria	1963-64	
3	Bangladesh	1993-94	
4	Belgium	1989-90; 1999-2000	(Revised)
5	Brazil	1994-95	
6	Belarus	1999-2000	
7	Bulgaria	1997-98	
8	Canada	1987-88; 1999-2000	(Revised)
9	China	1996-97	
10	Cyprus	1994-95	
11	Czechoslovakia	1986-87; 2001-2002	(Revised)
12	Denmark	1991-92	
13	Finland	1985-86; 2000-2001	Amending protocol
14	France	1996-97	(Revised)
15	F.R.G	1958-59	(Original)
	F.R.G.	1984-85	(Protocol)
	D.G.R.	1985-86	
	F.R.G.	1998-99	(Revised)
16	Greece	1964-65	
17	Hungary	1989-90	
18	Indonesia	1989-90	
19	Israel	1995-96	
20	Italy	1997-98	(Revised)
21	Japan	1991-92	(Revised)
22	Jordan	2001-2002	
23	Kazakistan	1999-2000	
24	Kenya	1985-86	
25	Libya	1983-84	
26	Malta	1997-98	
27	Malaysia	1973-74	
28	Muritus	1983-84	
29	Mongolia	1995-96	
30	Namibia	2000-2001	
31	Nepal	1990-91	

Continua

Brazil, Russia, India and China (BRIC)

Tax system structures and the effects on development and foreign trade performance - lessons and solutions

Continuação			
32	Netherlands	1990-91	
33	New Zealand	1988-89	
	(1999-2000 amending notification) (2001-2002 Supp. Protocol)		
34	Norway	1988-89	
35	Oman	1999-2000	
36	Philippines	1996-97	
37	Poland	1991-92	
38	Qatar	2001-2002	
39	Romania	1989-90	
40	Singapore	1995-96	
41	South Africa	1999-2000	
42	South Korea	1985-86	
43	Spain	1997-98	
44	Sri Lanka	1981-82	
45	Sweden	1990-91; 1999-2000	(Revised)
46	Switzerland	1996-97	
47	Syria	1983-84	
48	Tanzania	1983-84	
49	Thailand	1988-89	
50	Trinidad & Tobago	2001-2002	
51	Turkmenistan	1999-2000	
52	Turkey	1995-96	
53	U.A.E.	1995-96	
54	U.A.R.	1970-71	
55	U.K.	1995-96	(Revised)
56	U.S.A.	1992-93	
57	Russian Federation	2000-2001	
58	Uzbekistan	1994-95	
59	Vietnam	1997-98	
60	Zambia	1979-80	

Annex Table 1

Selected Macroeconomic Indicators, 2000-09

	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
National accounts	<i>(Percentage change)</i>								
Real GDP (at 1999/00 factor cost)	4.4	5.8	3.8	8.5	7.5	9.0	9.2	9.0	6.7
Consumption	1.8	5.4	1.2	7.0	6.9	..	..	..	..
Private consumption	2.1	6.2	1.6	7.8	6.5	..	..	..	..
Government consumption	0.3	1.7	-0.6	2.4	9.2	..	..	..	..
Gross fixed capital formation	0.0	5.0	9.9	11.3	9.5	..	..	..	..
Exports of goods and non-factor services	15.9	0.2	20.5	25.0	37.9	29.7	..	..	..
Imports of goods and non-factor services	8.1	-3.3	16.4	18.6	51.7	32.6	..	..	..
Unemployment rate (%)	7.3	..	..	..	8.3	..	..	..	..
Prices and interest rates	<i>(Per cent)</i>								
Inflation (%age change)									
WPI	7.2	3.6	3.4	5.4	6.4	4.4	5.4	4.7	8.4
CPI – industrial workers	3.7	4.3	4.0	3.9	3.8	4.4	6.7	6.2	..
Deposit rate ^b	8.5-9.0	7.5-8.5	4.25-6.0	4.0-5.25	5.25-5.5	6-6.5	..	..	..
Nominal prime lending rate (period average) ^c	11.5	11.5	10.8	10.3	10.3	10.3	..	..	..
Money credit (end period)	<i>(Percentage change)</i>								
Broad money supply (M3) ^d	16.8	14.1	14.7	16.7	12.3	21.2	21.5	21.2	18.6
Credit to a private sector	15.8	11.8	18.3	13.0	26.0	32.1	25.8	21.0	16.9
Exchange rate									
Rupee/US\$ (financial year - annual average)	45.7	47.7	48.4	46.0	44.9	44.3	45.3	40.2	45.9
Really effective exchange rate ^e (%age change)	5.3	-0.1	-4.9	1.5	2.5	5.4	-1.6	8.1	-8.3
Nominal effective exchange rate ^e (%age change)	0.3	-1.8	-6.3	-1.9	-0.7	3.9	-3.9	6.7	-13.0
	<i>(Per cent of GDP, unless otherwise indicated)</i>								
Central government balance									
Current balance	-4.1	-4.4	-4.4	-3.6	-2.5	-2.6	-2.0	..	..
Current revenue	9.2	8.8	9.4	9.5	9.8	9.7	10.3	..	..
Tax revenue	6.5	5.9	6.4	6.8	7.2	7.6	8.4	9.3	8.8
Current expenditure	13.2	13.2	13.8	13.1	12.3	12.3	12.4		

Continues

Brazil, Russia, India and China (BRIC)

Tax system structures and the effects on development and foreign trade performance - lessons and solutions

Continued									
Capital receipts	6.3	7.1	7.4	7.5	6.1	4.4	3.9	4.2	5.8
Capital expenditure	2.3	2.7	3.0	3.9	3.6	1.9	1.8	2.5	1.8
Gross fiscal balance ^f	-5.7	-6.2	-5.9	-4.5	-4.0	-4.1	-3.7	..	..
Central government total debt	..	59.9	63.4	62.8	63.8	61.5	62.6	..	..
Domestic debt	52.8	56.8	61.0	61.1	61.8	59.6	60.6	..	..
Saving and investment									
Gross domestic savings	23.4	23.5	26.4	29.7	31.7	34.2	35.7	37.7	
Public sector	-1.9	-2.0	-0.6	1.1	2.2	2.4	3.3	4.5	
Gross domestic investment	24.0	22.9	25.2	28.0	31.5	33.8	..	..	..
Public sector	6.9	6.9	6.1	6.3	7.1	7.4	..	..	..
External sector									
Current account balance	-0.6	0.7	1.2	2.3	-0.4	-1.2	-1.1	-1.5	-2.5
Net merchandise trade	-2.7	-2.4	-2.1	-2.3	-4.8	-6.4	-6.9	-7.7	..
Merchandise exports	9.9	9.4	10.6	11.0	12.1	13.0	14.0	13.5	..
Merchandise imports	12.6	11.8	12.7	13.3	16.9	19.4	21.0	21.2	..
Services balance	0.4	0.7	0.7	1.7	2.2	3.0	..	..	..
Capital account	1.9	1.8	2.1	2.8	4.0	3.1	5.0	9.2	..
Direct investment	0.9	1.3	1.0	0.7	0.9	1.1	2.4	2.8	..
Balance-of-payments	1.3	2.5	3.3	5.1	3.6	1.9	3.9	7.7	..
Terms of trade (1978/79=100)	128.1	125.4	113.6	123.4	110.0	135.0	142.0	163.0	..
Merchandise exports (%age change)	27.7	2.6	21.9	16.9	25.6	22.0	24.3	10.0	..
Merchandise imports (%age change)	10.2	1.4	16.2	17.8	45.3	30.3	24.4	15.5	..
Service exports (%age change)	9.4	9.6	22.9	22.7	57.3	40.5	..	..	..
Service imports (%age change)	32.1	-1.2	25.7	-7.2	62.6	33.4	..	..	..
Foreign exchange reserves ^g (US\$ billion, end-period)	39.6	51.0	72.6	108.8	137.0	145.9	192.4	299.6	..
in months of imports	8.2	10.9	13.4	16.1	13.7	11.1	..	..	..
Total external debt (US\$ billion; as at end-March)	101.3	98.8	104.9	111.6	133.0	138.1	169.7	221.2	..
Debt service ratio ^h	16.2	13.6	16.0	15.9	6.1	10.2	4.8	..	..

.. Not available.

a Provisional.

b Refers to the deposit rates of five major public sector banks of maturity of one to three years, as at end-March.

c Relates to States' bank prime lending rate, which is the benchmark interest rate for the various categories and classes of advances granted by the bank.

d Including currency with the public, other deposits with the RBI, demand deposits and time deposits.

e Six-currency trade based weight (including the EURO, Japan, United States, United Kingdom, Hong Kong and China).

f Revenue receipts plus capital receipts (not including borrowing and other liabilities) minus total expenditure.

g Excluding gold, SDRs (Special Drawing Rights) and Reserve Tranche Position in IMF.

h Including debt-servicing on non-civilian credits

Source: WTO. 2007, Government of India 2009 and Government of India 2009a;

Annex Table 2

Basic economic and social indicators, 2000-09

	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09
Real GDP at factor cost (Rs billion, 1999/00 prices)	18,647.7	19,729.1	20,477.3	22,225.9	23,896.6	26,045.3	28,711.2	31,297.2	33,393.8
Real GDP at market prices (Rs billion, 1999/00 prices)	20,308.7	21,366.3	22,162.6	24,022.5	26,022.3	28,424.8	31,200.3	34,027.2	36,094.3
Current GDP at factor cost (Rs billion)	19,254.2	21,001.9	22,653.0	25,494.2	28,559.3	32,509.3	37,793.9	43,208.9	49,331.8
Current GDP at market price (Rs billion)	21,023.8	22,810.6	24,580.8	27,654.9	31,266.0	35,671.8	41,291.7	47,234.0	53,217.5
Current GDP at factor cost (US\$ billion)	421.5	440.4	468.1	554.8	635.6	734.3	834.6	1,073.8	1,074.4
Current GDP at market price (US\$ billion)	460.2	478.3	507.9	601.8	695.9	805.7	911.8	1,173.8	1,159.0
GDP per capita at current market price (Rs)	20,631.7	21,975.5	23,299.4	25,773.4	28,684.4	32,223.8	36,950.2	41,416.1	..
GDP per capita at current market price (US\$)	451.6	460.8	481.4	560.9	638.4	727.8	815.9	1,029.2	..
Annual percentage change									
GDP by economic activity at constant 1999/00 prices									
Agriculture, forestry, and fishing	-0.2	6.3	-7.2	10.0	0.0	6.0	4.0	4.9	1.6
Mining and quarrying	2.4	1.8	8.8	3.1	7.5	3.6	8.8	3.3	3.6
Manufacturing	7.7	2.5	6.8	6.6	8.7	9.1	11.8	8.2	2.4
Electricity, gas, and water	2.1	1.7	4.7	4.8	7.5	5.3	5.3	5.3	3.4
Construction	6.2	4.0	7.9	12.0	14.1	14.2	11.8	10.1	7.2
Services	5.7	7.2	7.4	8.5	9.6	9.8	11.2	10.9	9.7
Trade, hotels, transport and communication	7.3	9.1	9.2	12.1	10.9	10.4	12.8	12.4	9.1
Financing, insurance, real estate, and business services	4.1	7.3	8.0	5.6	8.7	10.9	13.8	11.8	7.8
Community, social, and personal services	4.8	4.1	3.9	5.4	7.9	7.7	5.7	6.8	13.1
Per cent									
Share of main sectors in current GDP									
Agriculture, forestry, and fishing	23.4	23.2	20.9	20.9	18.8	18.3	18.2	18.1	17.5
Mining and quarrying	2.4	2.3	2.8	2.5	3.0	2.8	2.8	2.7	2.5

Continues

Brazil, Russia, India and China (BRIC)

Tax system structures and the effects on development and foreign trade performance - lessons and solutions

Continued									
Manufacturing	15.6	15.0	15.3	15.2	15.9	16.0	16.3	16.3	15.8
Electricity, gas, and water	2.4	2.3	2.4	2.2	2.1	2.0	1.9	1.8	1.6
Construction	5.8	5.8	6.0	6.2	6.5	6.8	8.4	8.7	8.9
Services	50.5	51.5	52.7	52.9	53.7	54.1	52.4	52.4	53.7
Trade, hotels, transport, and communication	22.3	22.8	23.3	23.9	25.0	25.4	25.1	25.2	25.3
Financing, insurance, real estate, and business services	13.2	14.0	14.7	14.7	14.5	14.3	13.9	13.7	14.0
Community, social, and personal services	15.0	14.8	14.8	14.3	14.3	14.4	13.5	13.4	14.4
Share of a sector in total employment ^a									
Agriculture, hunting, and fishery	5.1	5.2	4.9	5.2	5.3	5.6	5.5	..	..
Mining and quarrying	3.6	3.4	3.4	3.4	4.1	4.1	4.6	..	..
Manufacturing	23.7	23.2	22.9	22.2	21.5	21.2	20.9	..	..
Electricity, gas, and water	3.5	3.6	3.5	3.6	3.5	3.4	3.3	..	..
Construction	4.1	4.1	4.0	3.7	3.7	3.6	3.5	..	..
Services	60.0	60.6	61.3	62.0	61.9	62.0	60.9	..	..
Wholesale and retail trade	1.8	1.8	1.8	2.0	2.0	2.1	2.1	..	..
Transport, storage, and communication	11.3	11.2	11.3	11.2	11.0	10.7	10.2	..	..
Financing, insurance, real estate, etc.	5.9	5.9	6.0	6.7	7.1	7.3	7.6	..	..
Public administration and defense and other services	41.1	41.6	42.2	42.1	41.9	41.8	41.0	..	..
Memorandum ^b									
Birth rate (per 1,000)	26.1	25.4	25.0	24.8	24.1	23.8	23.5	23.1	..
Life expectancy at birth	63.3	63.3	63.7	63.3	64.0	64.0	..	..	..
Infant mortality rate (per 1,000 live births)	69.0	67.0	67.0	63.0	..	58.0	57.0	..	..
Adult illiteracy rate	42.8	42.0	38.7	39.0	..	..	..	..	..

.. Not available.

a Organized sector employment only.

b Based on calendar year: 2000/01 should read 2000.

Source: WTO, 2007, Government of India 2009 and Government of India 2009a;

4.2. Introduction to the Constitutional Law of India

Arnaldo Sampaio de Moraes Godoy*

The Indian right moves between tradition and modernity, bringing closer Vedic concepts, transcendent concepts of *dharma*, any references of significant population of the Islamic faith, any influences of a *common law* of England, starting a lively pluralism of sources¹. A democratic constitution was written, which should live and be applied to ancient idiosyncrasies, even indicative of the caste system, which enabled *pariahs*, untouchables and excluded. It is about a character made up over the centuries, though shaken and stimulated in the movement of opposition to England². The clash between ancient culture and political engineering is so new that gives the contours of the Indian constitutional law.

The constitution of India begins with the preamble which proclaims that the people of India solemnly decided to constitute the country into a Sovereign Socialist Secular Democratic Republic, in order to ensure to all citizens justice, liberty, equality and fraternity. This is a solemn declaration of 1949, the year of the constitution's promulgation.

It refers to the justice in its social, economic and political dimensions. It remembered the freedom in its thought, expression, belief and religion perceptions. The equality was conceived in terms of social status and opportunities. The fraternity was forearmed as a mechanism to ensure the dignity of individuals with the unity and the integrity of the nation in the consecrated expressions in the text to the comments coming, read in its English version.

India is organized as a union of states. The territorial composition of the country can be modified by legislation of the Parliament. States may have their territory increased or decreased, in addition to the changes in limits and even the name of the units. The Indian nationality is defined in a constitutional provision. Indians are those who were born in the territory of India, the children born in the territory of India, in addition to those who have resided in India in the five years preceding the making of the constitution previously mentioned. There are specific constitutional provisions, which reach Indians, who migrated to Pakistan. Indians living abroad has their Indian nationality, since they are registered at the competent diplomatic or consular department. It is excluded those who voluntarily acquired citizenship of another State, which consequently lose their Indian nationality by virtue of the constitutional provision. The Parliament has the jurisdiction to regulate other matters of nationality.

The constitution of India formally acclaimed isonomy. It has been written that the state may not deny to any person equality before the law as well as equal protection to

* Ex-General Coordinator for Tax Affairs of the National Treasury Attorney General in Brasília. PhD Researcher and Professor of the Masters in Law at the Catholic University of Brasília

¹ Cf. MENSKI, Werner F. *Hindu Law- Beyond Tradition and Modernity*. New York: Oxford University Press, 2005.

² METCALF, Bárbara D. e METCALF, Thomas R. *A Concise History of India*. Cambridge: Cambridge University Press, 2003, p. 260.

everyone within the territory of India. It has been determined that the State could not be discriminated against anyone based on religion, race, caste, gender or place of birth.

Access to stores, public restaurants, hotels and entertainment venues cannot be denied based on discriminatory practices. The same rule applies to the use of tanks, bathing sites, roads or any other items kept partly or entirely with State resources, and intended for the use of all the population.

This conception of equity is also projected by the constitution of India on employment relations, maintained by the State. The caste of untouchables was abolished, determining that untouchable is abolished and its practice in any form is forbidden. The use of this immemorial custom is a crime to be punished according to the law. The Constitution of India has abolished the use of noble titles, also forbidding the citizens of India from receiving securities from other States. Military and academic titles are an exception.

It is applied the freedom of expression, the right of peaceful assembly, the participation in unions and associations, the movement in the Indian territory, the choice of place of residence. India adheres to the legal reserve in criminal matters. It has also been explained that nobody will be compelled to testify against themselves. The human trafficking and the forced labor are forbidden and condemned. It is permitted, however, that the State imposes the law enforcement. There is an express provision in Indian constitution, which prohibits the employment of children under the age of 14 in factories or mines of the country, and in any other occupation that is harmful.

In terms of religion, it has been determined that subject to public order, morality and health, all religious denominations are entitled to keep their institutions for purposes of religion or charity, to conduct their own problems in matters of religion, to own and acquire movable and immovable property and to manage their properties in accordance to the law. It is forbidden the collection of taxes in favor of religious denominations. There is an article that protects the interests of minorities, with special attention to the admission in educational institutions maintained by the State. The right of maintenance of distinct languages, writing and cultures is validated.

Public policies should be targeted in order to equally ensure the citizens, men and women, the right to earn adequate livelihoods. It has been an objective that the ownership and the control of material resources of the community are distributed in order to better ensure the common good. The intention is to prevent the economic system to raise the concentration of wealth to the detriment of the common good. The wages are aimed to be the equal to men and women. Health and the strength of workers of both genders are pursued. Children are given opportunities and facilities for a healthy development, with conditions of freedom and dignity, ensuring childhood and youth against exploitation and moral and material abandonment.

It has been determined equality in the administration of justice and free legal advice for those who cannot afford lawyers' fees and court costs. The Indian Constitution provides brief requirements on labor protection, maternity, participation of workers in the decisions of the factories, the making of a civil code and the guarantee of free and compulsory education for children. It has been determined that it is a duty of the State to improve the level of nutrition and living conditions, as well as to improve public health.

It is also an obligation of the Indian State, under the constitution of that country, to organize national agriculture and livestock, to protect the environment by taking care of forests and wildlife, to protect monuments and sites of national importance, to effectively separate the judicial and executive powers and to promote international peace and security, among other determinations.

There is an article that states the basic obligations of Indian citizens. Every Indian must obey the constitution and laws, welcome and follow the noble ideals which inspire the struggle for national freedom, support and protect the sovereignty, unity and integrity of India, defend the country and provide services when asked, promote harmony and spirit of common brotherhood among all people of India, transcending barriers of religion and language, renounce to all forms of women's dignity denial, value and preserve the values of cultural heritage, protect the environment, including forests, lakes, rivers and wildlife, have compassion for living creatures, develop a scientific spirit, humanism, the spirit of research and reform, fight for the safeguard of public property, renounce violence, in addition to fighting for the excellence in all spheres of individual and collective activity, so that the Indian nation constantly reaches higher levels of effort and achievements.

The judiciary is headed by the President. The president is the one who also heads the armed forces. The President is elected by an electoral college which consists of members chosen by both houses of the legislature and the state legislative assemblies.

The presidential mandate lasts five years. Impeachment is expected when the president violates the constitution and the Indian constitutional text explicit every step of the procedure for removal. Re-election is allowed. It is required of a presidential candidate, among others, Indian citizenship and 35 year-old minimum age. The Indian constitutional text specifies the terms of the president's oath of office, namely: "I, [name of president], swear by God and solemnly affirm that I will faithfully serve in the position of President of India and make the best of my ability to preserve, protect and defend the Constitution and the laws and I will devote myself in service to the welfare of the people of India" The constitution also states a vice president, whose occupant heads a council of Indian states. There is special election for the post of the vice president, whose mandate, like the president, also lasts five years.

A council of ministers assists and advises the president. This council is headed by a Prime Minister. The prime minister is appointed by the president and other ministers are also appointed by the president, with advice of the prime minister. The Minister shall hold Office during the pleasure of the President. The Indian constitution provides an Attorney General, since the person appointed by the president holds the right conditions to assume the judiciary in the Supreme Court. This person has the competence to advise the Indian government in all legal matters.

The Parliament is bicameral; it consists of a Council of States and a House of the People. The Council of States has 12 members appointed by the president and with no more than 238 representatives of states and of the Union. The House of the People consists of no more than 530 members directly elected and no more than 20 members representing the Union territories, chosen in a manner provided by Law. It was determined that the parliamentary debates should be rendered into Hindi and English. The parliamentarian is

allowed to use his/her mother tongue, which, therefore, will be translated into Hindi and English.

The judiciary is, at the top the Supreme Court, headed by the chief judge, accompanied by seven other magistrates, unless the Parliament prescribes the greater number of judges. It is the president who appoints the judge of the Supreme Court. The magistrate cannot hold office after completing 65 years. Indian citizenship is required to hold the office of judge in the Supreme Court of India. The Supreme Court has jurisdiction to hear and adjudicate a conflict between the central government and other Indian states and between two states. The Supreme Court exercises judicial review and evaluates the process on final appeal.

1. References

- GLENN, H. Patrick. **Legal Traditions of the World**. New York: Oxford University Press, 2000. GODOY, Arnaldo Sampaio de Moraes. *Direito Constitucional Comparado*. Porto Alegre: Sergio Antonio Fabris, 2006. MENSKI, Werner F. **Hindu Law- Beyond Tradition and Modernity**. New York: Oxford University Press, 2005. METCALF, Bárbara D. e METCALF, Thomas R. **A Concise History of India**. Cambridge: Cambridge University Press, 2003. UNGER, Roberto Mangabeira. **Law in modern society**. New York: The Free Press, 1977. ZOLO, Danilo. **Cosmopolis- Prospects for World Government**. Cambridge : Polity Press, 1997. ZWEIGERT, Konrad e KOTZ, Hein. **Introduction to Comparative Law**. Oxford: Clarendon Press, 1998.

4.3. The Influence of India on Global Issues and its Relations with Brazil (Pronouncement)

Leila Bijos*

The last years have presented extraordinary results in terms of bilateral relations between Brazil and India, particularly in terms of scientific projects. Brazil has demanded efforts to expand its international relations with India, focusing on the growth of trade, exchanges in scientific projects, educational exchanges, among others.

The focus on new forms of economic integration makes clear that economic globalization is a new and fruitful frontier for the collective welfare, development and material progress. In this sense, the Minister of Trade and Industry, Kamal Nath, and Minister of Foreign Relations, Celso Amorim, met outside the Annual Meeting of World Economic Forum held in Davos, on January 30th, 2009, in order to identify possibilities for the resumption of trade negotiations of the Doha Round, and find joint solutions to the global economic situation.

The representatives of Brazil and India argue that it is necessary to prioritize the basic democratic values of dignity, freedom, respect for life and integrity of the human beings so that we can achieve qualitative parameters in the context of international relations, which have the human being as the primary purpose of democracy.

It is undisputed the participation of Brazil and India on issues of science, technology, environment, human rights, rights of women and children, housing and welfare for the population. The issues on the agenda illustrate the active participation of Brazil and India in a world of universal integration. Both countries have continental dimensions, with large populations, and face the common challenge of development. The objectives are ambitious in order to decrease the rates of endemic poverty, income disparities and the gaps in education with processes of institutional reform and economic opening, which will lead them to the establishment of continuous and dynamic developmental structures.

It is also worth noticing the importance of environmental conservation, another prominent topic in discussions between the two countries. Both countries share the unusual privilege of having abundant natural resources, with projects for the preservation of the environment that strive for conservation of tropical forests, fauna and flora, water resources, coupled with the material issue, the development of societies and quality of life of our nations¹.

*Leila Bijos holds a PhD in Sociology from the Universidade de Brasília (UNB), is a Professor of the Master course in International Economic and Tax Law from the Universidade Católica de Brasília, an expert on International Policy, a visiting researcher at the University of California in San Diego, USA, and at the University of Tsukuba, Japan.

¹ Marco Maciel, opening words at the Brazil-India Seminar, conducted on the 11th and 12th of January, 1996, in Rio de Janeiro.

Concerning the economic reform, India has overcome the challenge of terrorist violence and has delimited a controlled economic reform, according to the words of President Smt. Pratibha Devisingh Patil during a joint session of the Parliament in New Delhi, on February 12th, 2009². The Indian Government's diplomatic effort underlines the commitment of an articulated inclusive development in the National Common Minimum Program (NCMP), which was turned into laws, policies and programs. Among the most relevant actions, it is emphasized the right of labor for the population in rural areas, which was guaranteed by the National Rural Employment Guarantee Act and the Law of Social Security for Informal Sector Workers, 2008, which aims at facilitating the provision of social security for 430 million informal workers. Through the Law related to the Right to Information, the government has advanced toward community action, with a transparent public management, rendering the accounts to citizens.

The National Rural Employment Guarantee Act, which has already covered the entire country, is the first intervention of this type anywhere in the world, through which a country provides employment for a specific number of days for any category of citizen.

According to official figures, in 2007-2008, about 34 million rural families got a job under this program³. The program has the double objective of giving to the poor consumer spending and improving rural productivity and incomes.

In the sixtieth year of the republic, the National Rural Employment Guarantee Act makes India a Republic of Labor. The perspective that emerges in terms of radical changes in India shows that there is a new configuration of forces in international politics. Brazil, India, Russia and China, in a global sense, are considered as "new influential," and tend to exert increasing influence on global events contributing effectively to enforce law and order, ensuring international stability.

These coordinated efforts have significantly contributed to the resurgence of a new international order centered on common sense, on the perception of the interests of all countries, and on a perception of responsible and cooperative diplomacy. Gradually, India, like Brazil, has been actively imposing itself as a prominent member of the international community of "new influential," showing a serious work in the area of public and social policies.

² Official speech published by the newspaper Notícias da Índia, Vol. 3, Number 4, published by the Embassy of India, 02/15/2009, p.1.

³ Idem, p. 1.

