

"A STUDY OF THE IMPACT OF INCOME TAX ON THE REVENUE OF GOVERNMENT OF INDIA: AN EMPIRICAL ANALYSIS"

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Abstract:

This paper investigates Income tax is a critical component of the Government of India's revenue, contributing significantly to fiscal resources that fund public expenditure and development initiatives. This paper examines the impact of income tax on government revenue, focusing on trends, determinants, and economic implications from 1980-81 to 2024-25. Using secondary data from government reports and econometric analysis, the study explores the relationship between Income tax collections, tax policy reforms, compliance, and economic growth. Findings indicate that income tax revenue has grown steadily, driven by improved compliance, economic expansion, and digital tax administration. However, challenges such as tax evasion, a narrow tax base, and reliance on indirect taxes persist. The paper concludes that while income tax significantly boosters' government revenue, broadening the tax base and simplifying tax structures are essential for sustainable fiscal growth. Recommendations include enhancing tax compliance mechanisms and reducing exemptions to improve revenue productivity.

Keywords: Income Tax, Government Revenue, Tax Reforms, Indian Economy, Fiscal Policy

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Introduction:

Taxation is a cornerstone of fiscal policy, enabling governments to finance public goods, infrastructure, and social welfare programs. In India, income tax, as a direct tax, plays a pivotal role in revenue generation, contributing approximately 23% to total government revenue in FY 2023-24. This paper investigates the impact of income tax on the Government of India's revenue, analyzing its contribution, growth trends, and challenges. The study addresses three key questions:(1) What is the quantum of income tax revenue? (2) How does income tax contribute to total tax revenue? (3) What factors influence income tax collections? By leveraging secondary data and econometric insights, this paper provides a comprehensive analysis of income tax dynamics in India.

Methodology:

This study adopts a mixed-methods research design, integrating both quantitative and qualitative approaches to provide a comprehensive analysis of income tax revenue trends and reforms in India. The quantitative analysis is based on secondary data obtained from the Database on Indian Economy (DBIE) hosted by the Reserve Bank of India (RBI). Trends in direct tax revenue are closely examined, and key patterns and facts observed from the data are systematically presented.

Objectives:

- To analyse trends in income tax revenue over time.
- To assess the share of income tax in the total revenue of the Government of India.
- To examine the impact of income tax reforms on government revenue.
- To provide suggestions for enhancing income tax revenue.

Literature review:

Gupta, Lahiri and Mookharjee (1995) made an empirical analysis on income tax compliance in India from 1965-55 to 1992-93. They found that low tax rates, plethora of exemptions significantly affect the revenue collection. However, traditional enforcement tools like penalties had limited effects, suggesting the need for administrative reforms.

Gupta & Gang (2000) proposed a method for evaluating the impact of tax structure changes on tax revenue. They believed that revenue loss is the sum of tax rate effect, statutory base effect and evasion effect

Chattopadhyay, Das-Gupta (2002), in their article empirically studied the reaction of tax payers in respect to tax avoidance, compliance, tax planning, tax saving etc. in India. They have concluded that legal compliance costs effect tax collection positively and tax evasion negatively.

Lucotte (2012) made an empirical study on inflation targeting and tax revenue performance in 59 emerging countries. The paper concludes that adoption of monetary policy framework by maintaining inflation low levels encourages the government to improve collection of domestic tax revenue.

Acosta-Ormaechea and Yoo(2012), focuses on the relationship between tax structure and economic growth in specific Indian states. It found that property taxes and capital transaction taxes positively impacted state economic growth, while income tax and commodity-service tax had a negative effect.

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Sharma&Singh (2017), canvassed income tax responsiveness of India in post liberalization period from 1991 to 2015. It is derived from the paper that "The tax elasticity coefficient for the study period (1991-2015) has been 0.53, thus depicting the low magnitude of automatic responsiveness for income tax collections vis-à-vis variations in economic growth post the reforms era"

Mdanat, M., et al. (2018) argue that high income tax rates may deter savings and investment, reducing economic activity. In India, the tax-to-GDP ratio remains low compared to international standards, indicating untapped revenue potential. Recent data shows personal income tax collections grew by 17.47% in FY 2024-25, reflecting economic growth and improved compliance.

Kapoor, S., & Singh, A. (2023), limit of rupees 250,000 and tax rebates under section 87A for income up to rupees 500,000. highlights that India's tax system relies heavily on indirect taxes, with income tax contributing a smaller share due to a narrow tax base and tax evasion.

Data Analysis:

Empirical Analysis of Direct Tax Revenue

The empirical analysis is based on data from Table 1.0, which details the direct and indirect tax revenues of the Central and State Governments from 1980-81 to 2024-25 (Revised Estimates for 2023-24 and Budget Estimates for 2024-25). The focus is on the Central Government's direct tax revenue, primarily comprising income tax, to assess its impact on total government revenue.

Trends in Direct Tax Revenue

Direct tax revenue of the Central Government has shown remarkable growth over the study period. From Rs. 2,907 Crores in 1980-81, it increased to an estimated, Rs. 207,000 Crores in 2024-25, reflecting a compound annual growth rate (CAGR) of approximately 15.7%. Table 1 presents the direct tax revenue for selected years, highlighting key milestones.

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	Direct Tax Revenue (Rs. Crores)	Share of Total Revenue (%)
1980-8	1 2,907	22.1
1990-9	1 11,024	19.1
2000-0	1 68,306	36.3
2010-1	1 445,994	56.5
2020-2	1 944,875	46.8
2024-2	5 2,207,000	57.6

Table 1: Direct Tax Revenue of Central Government (Selected Years) Year

The growth can be segmented into distinct phases:

- 1980-81 to 1990-91: Slow growth (CAGR of 14.2%) due to a limited tax base and preliberalization economic constraints.
- 1991-92 to 2000-01: post-liberalization reforms led to a broader tax base, with direct taxes arising from Rs.15,207 Crores to Rs. 68,306 Crores.
- 2001-02 to 2010-11: Rapid economic growth and technological advancements (e.g., e-filing) boosted revenue to Rs 445,994 Crores.

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- 2011-12 to 2020-21: Revenue doubled to Rs. 944,875 Crores, despite a dip in 2020-21 due to the COVID-19 pandemic.
- 2021-22 to 2024-25: A sharp recovery, with a 49.2% increase from 2020-21 to 2021-22, reaching Rs. 2,207,000 Crores (budget estimate).

Contribution to Total Revenue

The share of direct taxes in the Central Government's total revenue has increased significantly, from 22.1% in 1980-81 to 57.6% in 2024-25. This shift reflects a move toward a more progressive tax system, with income tax playing a pivotal role. The decline in the relative share of indirect taxes (from 77.9% to 42.4%) further underscores this trend.

Interesting Finding

A notable observation is the 49.2% surge in direct tax revenue from Crores 944,875 in 2020-21 to Crores 1,408,293 in 2021-22, despite the economic disruptions caused by the COVID-19 pandemic. This rapid recovery suggests robust tax administration mechanisms, such as digital compliance systems, and a rebound in corporate earnings, warranting further investigation.

Visualizing the Trend

Figure 1 illustrates the growth trajectory of direct tax revenue over the study period, highlighting key economic events and policy reforms.

Figure 1: Trend of Central Government's Direct Tax Revenue (1980-81 to 2024-25)

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Table 1.0 Direct and Indirect Tax Revenures of Central Govt and State Govt (Rupees in Crores)

Year	Centre (gross)		States			Centre & States combined			
	Direct	Indirect	Total	Direct	Indirect	Total	Direct	Indirect	Total
1	2	3	4	5	6	7	8	9	10
2024-25	22,07,000	16,23,710	38,30,710	2,99,181	20,12,385	23,11,566	25,06,181	36,36,096	61,42,276
2023-24	19,45,000	14,83,411	34,28,411	2,59,462	17,69,040	20,28,502	22,04,462	32,52,451	54,56,913
2022-23	16,59,811	13,86,380	30,46,192	2,79,739	14,83,113	17,62,852	19,39,550	28,69,493	48,09,044
2021-22	14,08,293	12,94,892	27,03,185	1,22,343	13,34,886	14,57,229	15,30,636	26,29,778	41,60,414
2020-21	9,44,875	10,76,407	20,21,282	1,69,931	10,02,177	11,72,108	11,14,805	20,78,585	31,93,390
2019-20	10,49,549	9,58,030	20,07,579	1,66,654	10,57,348	12,24,002	12,16,203	20,15,379	32,31,582
2018-19	11,36,615	9,42,050	20,78,665	1,09,468	10,90,814	12,00,282	12,46,083	20,32,864	32,78,947
2017-18	10,02,037	9,13,456	19,15,494	1,19,152	9,43,488	10,62,640	11,21,189	18,56,945	29,78,134
2016-17	8,49,713	8,66,109	17,15,822	1,09,914	7,96,409	9,06,325	9,59,627	16,62,518	26,22,145
2015-16	7,41,945	7,08,013	14,49,958	88,176	7,58,967	8,47,143	8,30,121	14,66,981	22,97,101
2014-15	6,95,744	5,45,680	12,41,424	1,07,696	6,71,609	7,79,305	8,03,440	12,17,289	20,20,728
2013-14	6,38,542	4,95,541	11,34,083	88,231	6,24,231	7,12,462	7,26,773	11,19,772	18,46,545
2012-13	5,58,658	4,74,767	10,33,425	92,568	5,61,966	6,54,534	6,51,227	10,36,732	16,87,959
2011-12	4,93,947	3,91,232	8,85,178	77,299	4,80,274	5,57,573	5,71,246	8,71,505	14,42,752
2010-11	4,45,994	3,43,178	7,89,172	62,725	3,98,170	4,60,895	5,08,719	7,41,348	12,50,067
2009-10	3,77,487	2,43,881	6,21,368	47,387	3,15,856	3,63,243	4,24,874	5,59,737	9,84,611
2008-09	3,33,854	2,69,645	6,03,499	44,132	2,78,673	3,22,805	3,77,986	5,48,318	9,26,304
2007-08	3,12,243	2,79,104	5,91,347	43,446	2,42,703	2,86,149	3,55,689	5,21,807	8,77,496
2006-07	2,30,249	2,41,263	4,71,512	38,829	2,13,682	2,52,511	2,69,078	4,54,945	7,24,023
2005-06	1,65,249	1,99,398	3,64,647	30,179	1,81,768	2,11,947	1,95,428	3,81,166	5,76,594
2004-05	1,32,847	1,70,546	3,03,393	23,981	1,58,001	1,81,982	1,56,828	3,28,547	4,85,375
2003-04	1,05,090	1,47,658	2,52,748	20,213	1,35,138	1,55,351	1,25,303	2,82,796	4,08,099
2002-03	83,085	1,31,581	2,14,666	17,217	1,20,135	1,37,352	1,00,302	2,51,716	3,52,018
2001-02	69,197	1,17,177	1,86,374	15,679	1,06,894	1,22,573	84,876	2,24,071	3,08,947
2000-01	68,306	1,20,040	1,88,346	12,857	99,769	1,12,626	81,163	2,19,809	3,00,972
1999-00	57,958	1,13,794	1,71,752	12,979	86,813	99,792	70,937	2,00,607	2,71,544
1998-99	46,591	97,197	1,43,788	10,653	75,530	86,183	57,244	1,72,727	2,29,971
1997-98	48,274	90,946	1,39,220	6,352	68,800	75,152	54,626	1,59,746	2,14,372
1996-97	38,891	89,871	1,28,762	8,288	60,255	68,543	47,179	1,50,126	1,97,305
1995-96	33,563	77,661	1,11,224	7,913	53,603	61,516	41,476	1,31,264	1,72,740
1994-95	26,966	65,328	92,294	6,902	47,090	53,992	33,868	1,12,418	1,46,286
1993-94	20,298	55,445	75,743	5,012	41,015	46,027	25,310	96,460	1,21,770
1992-93	18,131	56,505	74,636	4,353	35,573	39,926	22,484	92,078	1,14,562
1991-92	15,207	52,154	67,361	3,840	31,568	35,408	19,047	83,722	1,02,769
1990-91	11,024	46,552	57,576	3,243	26,808	30,051	14,267	73,360	87,627
1989-90	10,005	41,631	51,636	3,023	22,838	25,861	13,028	64,469	77,497
1988-89	8,825	35,649	44,474	2,440	20,028	22,468	11,265	55,677	66,942
1987-88	6,748	30,918	37,666	1,917	17,467	19,384	8,665	48,385	57,050
1986-87	6,236	26,602	32,838	1,686	14,934	16,620	7,922	41,536	49,458
1985-86	5,563	23,107	28,670	1,401	12,919	14,320	6,964	36,026	42,990
1984-85	4,627	18,844	23,471	1,230	11,107	12,337	5,857	29,951	35,808
1983-84	4,320	16,367	20,687	1,017	9,498	10,515	5,337	25,865	31,202
1982-83	3,873	13,786	17,659	907	8,572	9,479	4,780	22,358	27,138
1981-82	3,552	12,264	15,816	843	7,377	8,220	4,395	19,641	24,036
1980-81	2,907	10,242	13,149	685	5,929	6,614	3,592	16,171	19,763

(Source: Budget documents of the Government of India and the State Governments.)

Notes: 1. Data for 2023-24 are Revised Estimates and data for 2024-25 are Budget Estimates.

2. States direct taxes, indirect taxes and total exclude States' share in Central taxes as reported in Central Government Budget documents.

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Conclusion

The empirical analysis reveals that direct tax revenue, driven by income tax, has become a cornerstone of the Central Government's fiscal framework. The consistent growth, accelerated by economic reforms and digitalization, underscores the importance of income tax in sustaining government revenue. However, its sensitivity to economic shocks, as seen in 2020-21, highlights the need for resilient tax policies

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