A Collaborative Mid-Term Strategy Meeting on

Creating a Tax Justice Narrative in India

Public Services International and **Centre for Budget and Governance Accountability**

Concept Note

Domestic resource mobilization is a central but often neglected element of development policy. National tax policies are integral to raising revenue for governments to invest in social security, make interventions across key social sectors, finance development, strive to reduce inequality and secure human rights.

India continues to be constrained by its low tax-GDP ratio of close to 17 per cent. The overall taxation rates in Asia at a regional scale are among the lowest in the world, below the tax levels in the European Union, the Americas, Africa and the Middle East.[1] The contribution of corporate tax to the tax mix in India has seen a decline, as corporate tax rates are lowered, even though profits accrued by multi-national corporations (MNCs) and big businesses have seen a significant increase. This is one of the factors leading to India's increasing dependence on indirect taxes, which form approximately two-thirds of the total tax collected in the country.[2] Indirect taxation is regressive in nature, as the proportion of one's income going towards consumption taxes tends to be higher at lower levels of income. A developing country like India also often engages in aggressive tax competition to create the perception of a conducive climate to attract foreign investment, which is reflected in tax exemptions to big businesses and MNCs, tax holidays and tax giveaways. These practices, together known as the 'race to the bottom', impede the mobilisation of adequate resources, and have led to the contractionary fiscal policy in the country.

Effective July 1, 2017, India has introduced a destination-based consumption tax, Goods and Services Tax (GST) which subsumes almost all indirect taxes at the centre and state levels previously levied on manufacturing of goods, sale of goods, imports and services. The GST has the potential to alter the landscape in India to a great extent. GST is expected to improve tax compliance and thus lead to an increase in tax revenue, has the potential to make the tax system simpler by bringing a myriad of indirect taxes under one umbrella, may significantly reduce the problem of cascading of taxes through its system of tax credit, and shift revenue to the states where the final sale of the good or service takes place rather than the manufacturing state. However, the impact of GST on smaller enterprises, activities in the informal sector and consumers would depend on the complex interplay of a number of factors; this would be clearer in the next few months, as the system is operationalised.

A number of challenges confront tax administration in India. Several departments at the centre and state levels are under-staffed and under-resourced. Shortage of trained human resource often leads to unresolved tax disputes, higher levels of tax litigation and limited information exchange, resulting in loss of revenue for the government. Reforms in tax administration in the country in the past few years have mostly been limited to enhanced technology and an emphasis on digitisation, along with strengthening of the powers vested in officers in the income tax department. However, the freeze on recruitment of staff

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[1] Martinez-Vazquez, Jorge. 2011. *Taxation in Asia*. Asian Development Bank

[2] Centre for Budget and Governance Accountability. 2017. *What Do the Numbers Tell? An Analysis of Union Budget 2017-18*

has not been reversed. The country also does not have an All-India Tax Litigation Cell, which delays resolution of tax disputes.

While progressive and effective national tax policies are vital to raising domestic resources, the secrecy mechanisms of the shadow financial system limit the ability of governments to raise revenue on their own. Illicit financial flows encompass the cross-border movement of money that is illegally earned, transferred or utilised, resulting from tax evasion, trade manipulation, organised crime, and corrupt payments to public officials in exchange for influence or access to resources; as well as tax avoidance by multi-national companies. Whether it is through anonymous companies or tax havens, or through the lack of effective information sharing between authorities across borders, illicit financial flows have a crippling effect on countries, especially developing countries.

Tax evasion, tax avoidance, crime and corruption are the broad components contributing to illicit financial flows. Depending on the country context, the degree to which each of those components is driving such illicit flows could differ. Some studies have suggested that developing countries primarily lose revenue due to trade misinvoicing through falsifying trade invoices and transfer mispricing through mispricing transactions between related business entities.

Data leaks in the last few years, such as the Panama Papers, Swiss Leaks and Lux Leaks point towards the underbelly of financial secrecy offered to the rich and powerful through tax havens. Aided by an efficient industry of tax lawyers, bankers, and accountants, tax havens are countries or jurisdictions that offer extremely low tax rates, secrecy in various forms, avoidance of financial regulations and criminal laws, and escape from corporate governance rules.

Even as reforms to fix these loopholes in the international tax system are being put forward, the design of global bodies currently setting the rules of international taxation, such as the OECD and the G20, has led to a systematic exclusion of developing countries from making the rules of global finance that affect them directly. The absence of an inclusive and global tax body also contributes to disparities between developed and developing countries. A well-resourced and inclusive intergovernmental tax body under the auspices of the United Nations has been a central demand of the G77 and supported by civil society.[3]

In such a context, Public Services International (PSI) and Centre for Budget and Governance Accountability (CBGA) are planning to organise a day-long mid-term strategy meeting for public sector trade unions and civil society organisations titled '**Creating a Tax Justice Narrative in India**' in **New Delhi** on **October 12, 2017**.

The meeting aims to further the discourse on the centrality of domestic resource mobilisation in the process of development, challenges facing tax policy and tax administration in India, issues of international taxation and financial transparency measures to challenge financial secrecy, and mapping the landscape of tax justice in India.

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[3] Inter Press Service. Developing Nations Seek Tax Body to Curb Illicit Financial Flows. August 8, 2016