Project Dissertation Report on

ANALYSIS OF IMPACT OF TAX INCENTIVES ON REVENUE

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CERTIFICATE OF ORIGINALITY

This is to certify that the project report entitled, "**ANALYSIS OF IMPACT OF TAX INCENTIVES ON REVENUE**" Submitted to Delhi School of Management, Delhi Technological University in the partial fulfilment of the requirement for the award of Masters of Business Administration is an original work carried out by Ravi under the guidance of Dr. Archana Singh.

The matter embodied in this project is a genuine work done by both to the best of my knowledge and belief and has been submitted neither to this University nor to any other University for the fulfilment of the requirement of the course of study.

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DECLARATION

I, Ravi, student of MBA 2020-22 of Delhi School of Management, Delhi Technological University, Bawana Road, Delhi – 42, hereby declare that the dissertation report "**ANALYSIS OF IMPACT OF TAX INCENTIVES ON GDP**" submitted in partial fulfilment of Degree of Master of Business Administration is the original work conducted by me.

The information and data given in the report is authentic to the best of my knowledge.

This report is not being submitted to any other University, for award of any other Degree, Diploma or Fellowship.

PLACE: Ravi

DATE:

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EXECUTIVE SUMMARY

Tax incentives may be described as any incentives that lessen the tax burden in an effort to set off them to make investments particularly initiatives or sectors. They are exceptions to the overall tax regime.

It is thus evident that tax incentives/ expenditures are developmental oriented tax concessions aimed to fulfil economic and social goals of the government by influencing the private decision making. The major purpose of tax incentives/expenditures is, however, to raise the aggregate levels of savings and investments and also to attract foreign investors.

While reading this topic I came across several research papers from which I came on a conclusion that to maximise gains, tax incentives must be carefully devised and implemented moreover adequate measures should be undertaken to provide favourable business environment in totality. But tax incentives in India are subject to various limitations as well as litigation.

For data analysis I have used Hypothesis test to measure the correlation and I have used Power BI for graphical presentation.

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Chapter 1

INTRODUCTION .

Increasing capital investment is one of the primary conditions of economic growth. In developing economies, we observe low levels of per capita income, high rate of consumption and consequently low level of savings and investment. Insufficient capital is one of the most crucial factors resulting in underdevelopment. Savings, which are the principal source of capital available for investment, form a very low percentage of the national income. Whatever little capital is available for investment is also not fully utilized due to hoarding habits of people and inadequate availability of entrepreneurs. Private foreign capital is shy in coming to these economies in the wake of lower rate of return. Foreign grants and loans are limited in amount and have, many a time, political strings attached with them. Therefore, modern welfare governments have to come forward to shoulder the responsibility of raising the level of savings and investment in the economy. It is in this context that tax incentives/ tax expenditures assume great importance.

The position of incentives in selling FDI has been the challenge of many research however their relative benefits and downsides had been truely stabilised. There had been a few superb successes in addition to tremendous disasters of their position as facilitators of FDI. As a thing in attracting FDI, incentives are secondary to extra essential determinants along with marketplace size, get right of entry to to uncooked substances and availability of professional labour. Investors normally have a tendency to undertake a degree system whilst comparing nations as funding locations.

Tax incentives may be described as any incentives that lessen the tax burden in an effort to set off them to make investments particularly initiatives or sectors. They are exceptions to the overall tax regime. Tax incentives could encompass as an instance decreased tax quotes on profits, tax holidays, accounting regulations that permit improved depreciation and loss deliver forwards for tax purposes, and decrease price lists on imported equipment, additives and uncooked substances or expanded price lists to shield the home marketplace for import substituting funding initiatives.

Because tax incentives are supposed to inspire funding in sure sectors or geographic regions they're not often furnished with out situations attached. Very regularly nations layout unique incentive regimes that element the tax blessings in addition to the important thing restrictions. For example those regimes can also additionally require that a facility be set up in sure areas have a sure turnover required the switch of era from overseas or rent a sure variety of individuals.

DEFINITION OF TAX INCENTIVES / TAX EXPENDITURES

There is no well established definition of tax incentives, but various authorities and authors have defined tax incentives in their own ways. Tax Incentives have been defined by the United Nations as,”....

reductions in the effective tax burden on the favoured activity as against the currently imposed upon it." According to Heller and Kauffman, " the most commonly encountered development oriented tax legislation..., are tax laws that reduce taxes for persons engaging in selected activity whose encouragement is considered of particular economic and social merit."

George E. Lent described tax incentives as those "tax concessions extended to induce the establishment of new business that otherwise would not be established, their nature, extent and duration, therefore, depend on a variety of considerations and would vary from country to country."

However, these definitions do not clearly indicate the purpose of tax incentives which is the distinctive element of such provisions. The tax burden can also be reduced through the provisions of rebates, reliefs and exemptions, the object of which is either to reduce the incidence of taxation in general or to remove certain anomalies or relax certain stringent provisions of the Act. The objective of incentive provisions is to encourage the tax payer to pursue a particular line of action. Tax incentives facilitate quick recovery of capital and a higher rate of return and, thus, induce domestic or foreign industrialists either to establish new businesses that would otherwise be not established or to expand their activities in already existing enterprises. In developing economies, such provisions may be said to constitute conscious attempts to use taxation as an instrument of promoting economic growth. Hence, the modus operandi of tax incentives may be the same as that of exemptions (full or partial), rebates or reliefs, deductions, deferrals, tax credits , tax holidays, etc, but the role of incentives provision has to be selective, flexible, substantial (in relief) and simple so as to maximise their effectiveness . Therefore, a high level of administrative capability and integrity is required forthe purpose and proper safeguards should be undertaken to prevent any misuse of such provisions. Otherwise tax incentives tend to be converted into tax loopholes. As the administrators are entrusted with policy judgements, they should also constantly gather andevaluate information with respect to their operations.

Tax incentives can also additionally as a substitute be termed as tax costs "such measures constitute opportunity sorts of authorities help and feature monetary implications just like the ones of direct costs... tax costs talk over with the sales foregone in the tax device".

The term „tax costs‟ refers to the ones provisions in a tax regulation that contain departures from the normative shape of the tax with the reason to inspire behaviour of tax payers in keeping with authorities targets or to alleviate hardships.10A tax expenditure, in huge terms, is, thus, a tax provision that deviates from a normative or a bench mark tax device. The normative or a bench mark tax shape does now no longer comprise any tax provision used to enforce authorities spending applications for favoured sports or groups." The tax costs idea recognises that a tax device incorporates additives which might be conceptually and functionally distinct, aleven though interwoven, withinside the tax laws. One issue incorporates the ones provisions important to enforce the normative tax shape; the opposite incorporates the ones provisions –the tax expenditure provisions- whose feature and impact are to enforce authorities spending applications".

In France," Any legislative or administrative degree can be known as a tax costs if its utility involves a lack of sales from the State, and consequently a lessening of taxpayers‟ burden in assessment to that which could have resulted below the “norms”. Similarly, withinside the U.S.A, tax costs are sales losses due to federal tax provisions that furnish unique tax remedy designed to inspire sure type of behaviour with the aid of using tax payers or to resource tax payer in unique circumstances.

As a result, the tax expenditure concept recognises three main elements in the revenue process: I imputed normative tax revenue from a normative tax structure, (ii) tax expenditures, and (iii) net tax revenue or tax revenue received. The following is the relationship between these three factors:

Net Tax Revenue/Tax Revenue Received=Normative Tax Revenue-Tax Expenditures.

However, not all tax expenditures are in the nature of tax incentives. Only tax expenditures relating to exemptions/rebates/reliefs designed to induce an activity or an individual to undertake or avoid certain course of action are termed as tax incentives. The concept of tax incentives as expenditures was first developed by Stanley S.Surrey in his capacity as Assistant Secretary of Treasury of U.S.A. He observed, Through deliberate departures from accepted concepts of net incomes and through various special exemptions; deductions and credits, our tax system doesoperate to affect the private economy in ways that are usually accomplished by expenditures- in effect to produce an expenditure system –described in tax language. This implies that for tax expenditure to be tax incentive, the direct purpose of the relief is to grant financial assistance to the desired sector or activity.

Here it is worth mentioning that all tax incentives are tax expenditures; they are designed to change behaviour to achieve particular economic and social targets. But not all tax expenditures are tax incentives. Tax expenditures could be used to subsidize particular tax payers. For example, tax subsidies that are used to reduce hardships are tax expenditures but they are not tax incentives.

OBJECTIVES OF TAX ICENTIVES/ TAX EXPENDITURES

By using the tax incentive device, the government intends to influence the resource allocation, investment pattern and the private decision making as a whole. Tax incentives stimulate mobilization of resources and guide the flow of these resources into desirable sectors ofthe economy. They pertain both to economic and social motives. "However, the main significance of tax incentives rests in their use to promote objectives associated with manufacturing operations." . In economies with relatively high tax rates, tax incentives help to reduce the negative consequences of the high tax rates. "The implementation of tax incentives for the aim of promoting industrial investment is based primarily on the assumption that the provision of tax benefits will inspire domestic or foreign investors to either start new businesses or raise their investments in existing businesses." Supporters of tax incentives assert that," by offering the correct incentives, there will be increased investment in the economy, generated from within and augmented by foreign investment flows... with free capital mobility. If a country does not match the tax incentives offered by neighbouring countries, there will be capital flight from the country as capital searches for areas offering the highest after the tax return".

Countries regularly hire a mixture of incentives to channel funding for improvement of a specific are or region. Regional improvement targets encompass help for rural improvement constructing business centres farfar from primary towns and decreasing environmental hazards, over urbanization and awareness of population.

Countries hire tax incentives in an effort to sell sectors of enterprise or sports taken into consideration vital for improvement. These can be centered at mining and business parks export-led sports the movie enterprise and groups with new technology.

The majority of tax incentives granted through growing international locations associated with funding in manufacture, exploration and extraction of mineral reserves, promoting of export and an increasing number of the tourism and amusement sectors. Developing international locations commonly do now no longer appeal to headquarters of corporations and carrier sports and consequently few international locations have incentives aimed toward a carrier sectors.

As mentioned earlier, incentives may be centered at many varieties of sports together with export promoting employment/abilities schooling home price brought and headquarters location. Free exchange zones (FTZs) commonly covers incentives for export- orientated manufacturing.

An vital goal of the use of incentives to draw funding to growing international locations is the switch of generation. Certain sort of tax incentives are designed especially for this purpose. Some growing international locations have added a particular set of incentives direct closer to studies and improvement (R&D) sports and generation initiatives.

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EFFECTS OF TAX INCENTIVES/TAX EXPENDITURES ON THE BUDGET

The following are the implications of tax expenditures:

- Tax expenditures have an impact on budget balance since they lower tax income. As a result, the overall budget deficit or surplus tends to rise or fall.
- They prioritise fiscal allocations because all tax expenditure programmes are given a higher budget priority by default. Tax expenditures have a greater priority than direct expenditure programmes in many developing nations, despite the fact that economic growth and poverty reduction are the primary goals.
- Tax expenditures impair the effectiveness and efficacy of governmental resource allocations. Some tax expenditures overlap or clash with direct spending, while others are outmoded, and diverse tax expenditures are not always coordinated.

- Tax expenditures add to the complexity of the tax system and make tax administration much more difficult. Abuseful tax payers would evade and avoid tax duties, creating more tax revenue loss, by taking advantage of the convoluted tax system and overburdened tax administration.

- Government officials and politicians can take advantage of tax expenditures that are loosely governed by financial discipline, either for personal gain or to assist favoured interests.

FISCAL ACCOUNTABILITY AND TRANSPERANCY

Because tax prices are authorities spending (channelled thru the tax system), they ought to be challenge to the equal duty and transparency standards as direct prices. Under the world over regularly occurring principles, economic duty calls for that the State ought to be held accountable via way of means of its human beings and elected our bodies for its monetary desire and for its moves in the use of public funds. Transparencies in authorities operations have numerous dimensions. At the mixture level, transparency calls for provision of dependable facts at the authorities‟s economic coverage intentions and forecasts. This ought to be found out thru designated records and facts, along with ebook of complete price range documents. Further, transparency predicted from the authorities additionally necessitate readability at the shape and features of authorities , public availability of complete facts and monetary records which ought to meet the regularly occurring excellent wellknown and ought to be subjected to unbiased audit scrutiny.

There are exceptional techniques of estimating and projecting tax prices. These encompass sales foregone, sales advantage and outlay equal techniques. However, in maximum international locations sales foregone approach is typically advocated and accompanied for estimating tax prices. Revenue foregone is described as the quantity via way of means of which tax sales is decreased due to the life of a specific provision. It is primarily based totally upon a contrast of the present rules and the rules with out tax provision in question. It is an ex-publish degree of the price of a specific relief. Under tax sales foregone approach, the price of tax expenditure is expected because the deviation among the tax paid via way of means of taxpayers stricken by a particular tax provision and tax paid via way of means of comparable tax payer now no longer stricken by that provision. Nevertheless, we need to now no longer overlook that this approach additionally has a few limitations. It does now no longer consider modifications in taxpayer‟s behaviour. This approach estimates tax prices one at a time. It does now no longer account for the alternate whilst one provision is eliminated which may also bring about extended use of different provisions or decreasing tax sales elsewhere. Further, it's miles viable that elimination of tax expenditure may also bring about a few taxpayers entering into a better marginal tax bracket beneathneath a revolutionary tax system. The tax expenditure approach does now no longer consider such modifications. Despite those limitations, sales foregone approach continues to be the nice viable approach to be had to estimate the price of tax expenditure. However, it ought to be saved in thoughts that during estimating and projecting tax prices, a dependable records base is a first-rate element in making sure the reliability of estimates.

Nevertheless, it ought to be saved in thoughts that “tax incentive legal guidelines do now no longer perform in isolation... They feature in terms of a given financial and political framework, an present underlying tax system, and the tax structures of the international locations”. 16Therefore, such different elements as non-tax rules affecting funding, present funding pattern , attitudes and prospects, the authorities‟s different financial guidelines and its abilties for forwarding financial development, and its capability to preserve financial and political balance need to be taken into consideration in any prediction approximately the viable effect of incentives.

GENERAL CHARECTERISTICS OF TAX INCENTIVES/TAX EXPENDITURES

Relief through tax incentives/tax expenditures may be provided by the way of exemptions/ exclusions from income, deductions from gross income, tax rebates, tax credits or even refunds. Special rates may be applicable in certain other cases. Since under tax incentives/tax expenditure, assistance is provided through reductions in tax liability rather than direct aid, they are qualified as tax expenditures. Whatever may be the mode of operation, these incentive provisions have following distinctive features:

1. Tax incentives/Tax expenditures are optional

The operation of tax incentives/tax expenditures is based on the principle of motivation or persuasion and not on coercion or force. Incentives are provided for voluntary activities at the choice of the tax payers.

2. Tax Incentives/Tax expenditures are specific

Tax incentives/tax expenditures are designed to meet specific objectives. Motives behind tax incentives are varied. Such incentives are granted for mobilization of savings, raising investments, directing investments to priority sectors, attracting foreign capital and encourage scientific research and development. Many a time, welfare measures are also undertaken throughincentives.

3. Tax Incentives/Tax expenditures are selective

Tax incentive/tax expenditures legislation applies to only those incomes or wealth relating to particular activity, industry or assessees, the activities which the government intends to encourage. At times incentives are restricted to certain regions only.

4. Tax Incentives/Tax expenditures are temporary

Tax incentives/tax expenditures are enacted for specific purpose. Once the objective is fulfilled or they fail to fulfil the associated objective, they become obsolete and they are scrappedfrom the statutes. Thus, the inventory of tax incentive provision keeps on changing from time to time.

5. Tax Incentives are Exogenous to the Basic Tax Structure

Tax incentives/tax expenditures are not a part and parcel of the tax structure. They are exogenous to the basic tax structure and can be deleted/added without affecting the working of tax as an instrument of mobilizing revenue.

CLASSIFICATION OF TAX ICENTIVES/TAX EXPENDITURES

Tax incentives/tax expenditures are of various types and are provided to fulfil various objectives and they operate through different mechanisms. From this view point, incentives may be classified on the following three grounds:

I. On the basis of delivery mechanism
II. On the basis of objectives
III. On the basis of economic considerations

(i) On the Basis of Delivery Mechanism

From the angle of delivery mechanism tax incentives/tax expenditures are classified into following four parts-

(a) Exclusions from Income: Certain incomes are excluded from being included in the gross income either totally or partially. In some cases, exclusion may grant permanentrelief from taxation while in other cases it may simply defer taxes to a later date. For instance contribution to a certain fund may be excluded initially but may be subject to taxation at the time when lump sum payment are made to the contributor at the time of maturity (EET Method). The mechanism of exclusions applies both on individual incomes and corporations. Under this method, revenue losses cannot be calculated simply because such contribution are excluded from computation of income and are not recorded in the incometax returns.

(b) Deduction of Certain Payments or Income from the Gross Total Income:

Deductions are fixed amounts of income or certain specified expenditures which Would otherwise be included in taxable income. In most cases, deductions representdirect and permanent tax reductions. As deduction is granted form the top layer of

income, relief is directly proportional to the marginal tax rate of the tax payer. In some

cases deduction is a onetime deduction while in other cases it is spread over several years. The device of deduction is used widely both in the case of individual incomes and corporate incomes However, such mechanism hamper the vertical equity of the tax system.

(c) Credit Against Tax, Tax Rebates, Refunds: Tax credits or tax rebates are tax relief measures relating to tax amount due, viz they provide deductions from the tax amount due oralternatively as refund of tax paid. This category of tax incentives eliminates the effect of benefit being determined by the tax payer‟s marginal tax rates as observed in the earlier two classes of incentives. Relief provided in this case is a fixed proportion of all assesses, irrespective of the marginal tax rate. Since credit is granted against the tax liability it can be availed only when sufficient tax liability arises to absorb the credit, otherwise the credit will go unutilised. For example, in the Union Budget for 2013-14 , the Finance Minister provideda tax credit of Rs.2000 to every person who has a total income up to Rs.5 lakh and it is hoped that 1.8 crore tax payers will benefit to the value of Rs.3600 crore (Para 125 of the Budget speech)

(d) Special rates of Tax or Statutory Reductions of Tax rates: This is perhaps the simplest mode of granting relief to tax payers. Assesses are subject to lower than usual rates of taxation-thus providing a straight forward relief.

(ii) On the Basis of Objectives

Each incentive/expenditure is designed with a view to fulfil or realise a particular objective or even multiple objectives-the ultimate goal being that of accelerating and assisting the process of economic development. The various objectives for which tax incentives are granted are the following:

(a) Incentives for Savings and Investment: The primary objective of tax incentive /tax expenditure legislations is increasing the levels of savings and investments in the country. These incentives are also designed to direct the flow of investible funds into priority/desired channels.

(b) Incentives for enhancing Exports and Foreign Exchange Earnings: In developing economies, adequate foreign exchange reserves are vital to finance essential imports. Any deficiency on this account can create supply bottlenecks. In a developing economy, tax incentives/expenditures for boosting foreign exchange earnings are significant as exporters face various sorts of bottlenecks usually due to inadequate infrastructure, inferior quality or inadequate inputs at uncompetitive prices. To induce investors to engage in export orientedunits, export promotion has become a major objective of tax incentive legislations.

(c) Incentives for Research and Development: Certain tax incentives/tax expenditures aim at encouraging research and development in order to develop indigenous technology. This leads to better utilization of capital and better Incremental Capital Output Ratio (ICOR). Import of technology leads to drainage of valuable foreign exchange.

(d) Incentives for Balanced Regional Development: Less developed economies are marked by regional disparities. Presence of industrially backward regions obstructs the process of rapid and all around economic development. Industrialisation of these regions is an essential prerequisite to raise level of development of the economy as a whole.

(e) Incentives for Agriculture and Rural Development: Agriculture and rural development are complimentary in nature since agriculture is primary occupation in rural areas. Support to agro-based and agro-processing industries is a major objective of tax incentives.

(f) Incentives for Welfare Motives: Development of social sector is intricately interwovenwith the material progress of the economy. Development of human capital requires adequate facilities for education, health, family planning, conservation of natural resources,maintaining the balance of ecology, etc. Benefits of economic development may not tickle down to social sectors. Therefore, tax incentives/tax expenditures seek to directly encourage social sector development.

(iii) On Basis of Economic Consideration

(a) Investment Linked Tax Incentives: The investment linked incentives are so termed as they are dependent upon actual investment being made in the industrial sector in general, in selected industries or in backward areas.

(b) Expenditure–Linked Tax Incentives: These incentives relate to specific expenditures already incurred. These incentives may be further sub-divided into expenditure relating to actual operations of business and those relating to programmes of economic or national importance.

(c) Profit-Linked or Income-Linked Tax Incentives: Such incentives are linked to specific incomes-for instance, profits from priority industries or from small scale units etc.

Issues relating to the Tax incentives/ Tax expenditures

(i) Tax incentives/expenditures are inequitable and regressive in nature

Tax incentives/tax expenditures provide greater relief to the higher brackets since exemptions and deductions are made from the top layers of the income. They are highly regressive in nature when applied on personal income because personal income tax is characterised by progressive slab system. Even in case of corporate incomes where a flat rate in levied, they amount to a higher total relief for a higher profit making companies. Besides, tax incentives do not benefit those who are outside the tax system because their incomes are low or they are having losses. Tax incentives distort both horizontal and vertical equity. Although this criticism seems valid, we cannot deny that the developmental needs, may, at times, are of greater priority than equity. The favourable treatment of tax payers is always subject to performance of certain desirable activities only.

(ii) Tax incentives/expenditures keep the tax rate high by contracting the tax base and reduce revenues

It is often alleged that tax incentives/tax expenditures lead to shrinkage of tax base and loss of revenue, due to which pressure is created to keep the statuary tax rates high. We know that high tax rates are themselves detrimental to developmental purposes as they discourage savings and investment. Tax incentives/tax expenditures, thus, become counterproductive and benefits accruing from them are lost on account of disincentives created by high statutory rates of taxation. However, it can also be argued that tax incentives are also in the nature of expenditures and if the government has had employed direct assistance rather than tax concessions even then the government treasury would have suffered a similar loss of revenue. Therefore, the criticism does not apply to tax incentive technique as such. Furthermore, the knowledge of Laffer‟s curve indicates that a moderate level of tax rates generates the optimum amount of revenues, which will be valid even if tax incentives are retained.

(iii) Tax Incentives/expenditures distort allocation of resources

Tax incentives distort the choices of market place and lead to inefficiency in the whole production process."It is interesting to note that, even within the area sought to be benefited by the tax incentives, the design of the incentive may push or pull in unneutral directions, which may or may not be desirable." Further, the impact of tax incentives /tax

expenditures on the allocation of resources is an intended one. Allocation of resources as determined by market forces may not always be the most desired one specially in a planned economy as it is the government‟s prerogative to decide which allocation is the best for fulfilling national priorities.

(iv) Tax Incentives/expenditures permit windfall by paying tax payers for doing what they would do even otherwise

It is generally alleged that tax incentives/tax expenditures are wasteful because some of the tax benefits go to tax payers for activities which they would have performed without such benefits. However, it is very difficult to determine actually whether the tax payer would have undertaken the activity in the absence of tax benefit or not, but to some extent this criticism is definitely valid.

(v)Tax Incentives/expenditures make tax laws complex

Tax incentives/tax expenditures are exogenous to basic tax structure. They are additional legislations devised to fulfil certain developmental purposes, but in the interest of doing so the normative tax structure gets distorted with respect to its efficiency and simplicity. Tax incentives/tax expenditures open up new loopholes facilitating evasion of large scale revenues. They also impose additional burden on tax administration.

Exemptions & Deductions

Exemptions and deductions available under the Act may broadly be grouped as under :

a) Tax-free income [sec, 10,10A,10B,10BA,and 13A]
b) Deductions from gross total income [secs. 80C to 80U]

Tax- free incomes [Secs. 10&13A]

The following incomes are exempt from taxation under sections 10 and 13A :

- [clause (1)] Agricultural income
- Payments from family income obtained by a Hindu Undivided family member [clause (2)].
- [clause (2A)] Profit share from the enterprise.
- Interest on regulated securities received by a non-resident [clause (4)].
- Interest on sums credited in the Non-resident external account received by a person who is not a resident of India [clause (4)].
- An employer's leave travel concession to an Indian citizen employee [clause (5)].
- All types of remuneration obtained by foreign ambassadors [clause (6)].
- Salary paid to a foreign person working for a foreign company in India if his stay in India is less than 90 days [section (6)(iv)].
- Salary obtained as a member of a ship's crew by a non-resident foreign person whose total stay in India does not exceed 90 days [article (6) (viii)].
- Remuneration earned by a foreign government employee deputed in India for training in a government establishment or public sector undertaking [clause (6)(xi)].
- [clause (6A)] Tax paid on behalf of foreign corporations.

- In the event of a non-resident/foreign corporation, tax paid by the government or an Indian enterprise [clause (6B)].

- designated foreign firms' income from services performed in or outside India in projects related to India's security [section (6C)].
- Any money received as a result of allegiance from the National Technical Research Organization by a non-resident/foreign enterprise [clause (6D) from the assessment year 2018-19].
- a stipend paid by the Indian government to its workers stationed abroad [clause (7)].
- Non-resident consultants' and their foreign employers' remuneration/fees [clauses (8A) AND (8B)].
- Death and retirement benefits are subject to the limitations set forth in paragraph 12.2 [clause (10)].
- Commuted pension value, subject to the limitations set forth in paragraph 12.3 [clause (10A)].
- [clause] Leave salary (10AA).
- Compensation for retrenchment [clause (10B)].

- Compensation obtained by an individual or his legal successor from the federal government, a state government, or a local government as a result of a disaster [clause (10BC) applicable from the assessment year 2005-06].
- Compensation from a government agency at the time of voluntary retirement or separation [clause (10C)].
- Employer-paid non-monetary perquisite tax [clause (10CC)].
- [clause (10D)] Any sum (including bonus) on a life insurance policy.
- [clause (11)] Any amount from the statutory or public provident funds.
- To the extent that it is authorised under a rule 8 of Part A of the Fourth Schedule [clause (12),

accumulate balances due and becoming payable to an employee from a recognised provident fund.

- Withdraw from NPS in part [paragraph (12B)].
- Amount paid to the employee's legitimate heirs from an approved superannuation fund [clause(13)].

House rent allowance [clause (13A)] is subject to certain limitations

Concluding Observations

It is thus evident that tax incentives/ expenditures are developmental oriented tax concessions aimed to fulfil economic and social goals of the government by influencing the private decision making. The major purpose of tax incentives/expenditures is, however, to raise the aggregate levels of savings and investments and also to attract foreign investors. Other objectives include export promotion, employment generation, area development, research and development and welfare provisions. These tax concessions may be provided inthe form of exemptions, deductions from gross income or as tax rebates.

The device of tax incentives has been both defended and opposed by economists. The main argument in favour of tax incentives is that they do not require any separate administrative machinery and through them the government can delegate some of its decisions making to private sector to achieve it various objectives. But, they have also been opposed due to their influence with the tax structure. However, it would be unwise to abolishtax incentives/tax expenditures totally. The government policy should, in fact, be a judiciousmix of both the tax expenditures and direct expenditures techniques.

Chapter 2

REVIEW OF LITERATURE .

Theoretical concepts reveal that any economic activity is influenced by some fundamental factors. Tax considerations play a significant role in influencing variables such as savings, investments, etc. However, the actual working of tax incentives/tax expenditures has remained controversial, mainly because it is not possible to accurately isolate the impact of tax incentives/ tax expenditure from the impact of multiplicity of other factors. Various studies have been conducted from time to time which reveal some trends and generalisationsregarding effectiveness of tax incentives/tax expenditures. Some of the important studies are as under:

1. **J.Heller and K.M.Kauffman**, in their book described the variety of tax incentive devices and the administrative problems associated with their use. They have given a systematic description of tax incentives and have opined that where selective tax incentives are granted, a high degree of administrative proficiency is required. The book describes and evaluates a few widely used tax incentives and provides guidelines for the policy makers to reform and implement tax incentives statutes. To maximise gains, tax incentives must be carefully devised and implemented.

2. In this study, **Paul L Chen Young** tries to appraise the results of Jamaica‟s experience with tax incentive policies. Recognising that there are costs and benefits from granting tax incentives, the paper attempts to measure these benefits and costs to the government and the economy. The author suggests that adequate measures should be undertaken to provide favourable business environment in totality, tax incentives should not be biased against local investors vis-a-vis foreign investors and emphasis should be laid on coordination of trade and fiscal policies.
3. **Robert Eisner**, in his paper discusses the impact of tax incentives in the U.S.A, with special reference to liberalised depreciation, equipment tax credit and capital gainsexclusions. The author observes that special treatment of capital gains offers a bias in favour of corporate enterprise and corporate equity. The author feels that such measures interfere with free market forces and misallocate resources so as to reduce output and growth. They also redistribute income from working people to property owners. He, therefore, argues against tax incentives in a free economy.
4. **Anand P. Gupta**, in his study compares tax holiday and development rebate. He observes that unlike development rebate, tax holiday is neutral to capital technology. He concludes on the basis of his study that benefits from tax holiday are very small due to long gestation periods, whereas , the development rebate has been found to be contributing to the liquidity and growth of industry.

5. **MadhurSrinivas**, in his working paper analyses the effect of income taxation on household savings in India and opines that income tax can have significant effects on household savings both through disposable income channel and interest rate channel.The author finds substantial interest elasticity of savings and goes on to conclude that reduction in tax on interest income can lead to a substantial increase in household savings.

6. **Chelliah Committee**, According to the Interim Report, India has a multitude of tax incentives incorporated into its income tax code, with a considerable number of them remaining in place. Many incentive clauses have been demonstrated to have a minimal effect, according to studies. Furthermore, there are frequently no means of quantifying or validating the extent of the benefit obtained from each of the provisions, and both the cost and the benefit to society are unknown. The complexity of the requirements, which include a variety of restrictions and specifications to prevent misuse, makes administration and compliance difficult.

   Furthermore, deductions frequently impose overly substantial tax benefits on taxpayers with higher incomes, which diminishes the tax system's progressivity as well as horizontal fairness, and tends to skew resource allocation. "If the income tax system is to be made simple, equitable, and least distortive, and the rates are to be decreased substantially," the Committee continues, "most concessions and deductions, except for costs of earning, should be deleted."

7. In their paper, **Mahima Sharma and A.K.Jain** has opined that in developing countries, the role of foreign investments is particularly desirable to bridge the savings-investment gap and to induce advanced technology in the production process. Tax incentives reduce the outgo through tax payments and result in a higher net rate of return. The authors goes on to conclude that, " The working of tax incentives in India require to be fine tuned in certain respects to realise greater overall benefits as againstthe costs in the form of distortionary effects and losses in revenue. "

8. After examining the various tax incentives for saving in detail, the **Kelkar Committee** concluded that there is no significant empirical evidence to support the hypothesis that tax incentives facilitate higher financial savings (by the private sector) at the macro level. The incentives stimulate not only saves, but also the transfer of cash from one type of investment to another, and that for the sole purpose of locking up these monies for a limited time. The netting principle does not apply, therefore dis-savings are tax-free. The Task Force goes on to say that in any incentive structure, it's best if the incentives being promoted have broadly similar rates of return.

9. In their paper , **Anil Kumar Jain and Parul Jain** have tried to analyse tax incentives on the basis of delivery mechanism and have reached the conclusion that India"s experience reveals that there has been defects associated with the use of tax incentive legislation as well as the operation and implementation of such incentives. The authors conclude that tax incentives, despite certain drawbacks, need to be retained in the Indian tax system. The authors suggest that tax incentives should not be open-ended but should be linked to performance, they should be coordinated with other policy measures, tax administrators should ensure that tax incentives do not end up being tax loopholes, there should be stability in tax incentive provisions and data in respect of each item ofdeduction should be computed separately for different ranges of returned income.

10. **Carlo Garbarino** created a framework for comparative analysis of tax incentives in his article by using a methodology based on the circulation of tax incentive models that are regarded policy alternatives for tax design for development. He also used a political economy approach to examine the influence of tax incentives, concluding by demonstrating patterns of partial convergence and competitive pressures in the circulation of tax incentive models.

11. **Simon Munongo and Zurika Robinson** attempted to examine the impact of tax incentives in luring FDI in their paper. Their research looked at both theoretical and empirical literature, as well as the benefits and drawbacks of tax incentives. Finally, the authors found that, while tax incentives are significant in attracting FDI, they are more effective when paired with non-tax variables. Macroeconomic conditions, infrastructure, and solid institutions, they believed, are additional crucial

non-tax elements that boost an economy's attractiveness to FDI.

Concluding Observations

To maximise gains, tax incentives must be carefully devised and implemented moreover adequate measures should be undertaken to provide favourable business environment in totality. But tax incentives in India are subject to various limitations as well as litigation. Madhur Srinivas added that substantial interest elasticity of savings and goes on to conclude that reduction in tax on interest income can lead to a substantial increase in household savings. Whereas Kelkar Committee concluded that there is no significant empirical evidence to support the hypothesis that tax incentives facilitate higher financial savings (by the private sector) at the macro level. While tax incentives are significant in attracting FDI, they are more effective when paired with non-tax variables.

Chapter 3

RESEARCH METHODOLOGY .

Objectives of the Study

The objective of the study is to identify the relationship between tax incentives and Revenue.

Hypothesis

The following are the null and alternate hypothesis in reference to this study –

H_{01}- There exist no significant relationship between tax incentives and the GDP

H_{11}- There exist a significant relationship between tax incentives and the GDP.

Methodolgy :

Data is collected from Budget Receipt of 2018-2019 and 2019-2020 from the annexure 7 for Statement of Revenue Impact of Tax Incentives under the Central Tax System: Financial Years 2016-17 and 2017-18 which is available on indiabudget.gov.in. Then revenue is measured by hypothesis testing.

FINDINGS

Sl. No.	Nature of Incentive	Revenue Impact (in Rs crore) [2016-17]	Projected Revenue Impact (in Rs crore) 2017-18	Revenue Impact (in Rs crore) 2018-19	Projected Revenue Impact (in Rs crore) 2019-20
1	“Deduction of export located in	19,695.99	21,882.02	22,889.65	23,539.72
	SEZs (section 10AA)				
2	Accelerated Depreciation (Section 32)	66,350.44	64,868.81	54,278.39	55,819.90
3	Deduction/Weight for expenditure on scientific research (Sec 35 (1),(2AA) &(2AB))	11,263.91	11,012.39	8,080.47	8,309.95
4	Deduction on eligible projects or schemes for the social and economic uplift of the public (Sec 35AC)	299.13			
5	Deduction in respect of specified business (Sec 35AD)	1,725.82	1,917.37	3,953.81	4,066.09

6	Deduction on account of donations to charitable trust and institutions (Sec 80G)	1,434.32	1,593.51	2,446.79	2,516.27
7	Deduction on account of contributions to political parties (Sec 80GGB)	103.07	114.51	814.54	837.67
8	Deduction of profits undertakings engaged in development of infrastructure facilities (Sec 80-IA)	6,944.90	7,715.71	4,973.43	5,114.67
9	Deduction of profits of undertakings engaged in development of SEZs and industrial parks (Sec 80-IA)	290.22	322.43	467.30	480.57
10	Deduction of profits of undertakings engaged in providing telecommunication services (Sec 80-IA)	275.04	305.56	1.39	1.43

11	Deduction of profits undertakings engaged in generation transmission and distribution of power (Sec 80-IA)	11,688.31	12,985.58	13,231.70	13,607.48
12	Deduction of profits of undertaking engaged in revival	151.73	168.57	76.08	78.24
	of power plant (Sec80-IA)				
13	Deduction of profits undertaking engaged in development of SEZ Act ,2005(Sec 80-IA)	1,676.62	1,862.71	1,097.76	1,128.93
14	Deduction of profits of eligible start-ups (Sec80-IA)	0.26	0.29		
15	Deduction of undertakings located in Jammu & Kashmir (Sec80-IB)	143.50	159.42	58.32	59.98

16	Deduction of profits of industrial undertakings located in industrially backward states other than Jammu& Kashmir (Sec80-IB)	4.95	5.50	1.96	2.01
17	Deduction of profits of industrial undertaking located in	0.87	0.96		

	drawback district (Sec 80-IB)				
18	Deduction of profits of industrial undertakings derived from production of minerals oil and natural gas (Sec 80-IB)	1,876.22	2,084.46	1,342.78	1,380.91
19	Deduction of profits of industrial undertaking derived from	65.27	72.51	26.11	26.85
	housing projects (Sec 80-IB)				
20	Deduction of profits of industrial undertakings derived from operating a cold chain facility (Sec 80-IB)	16.45	18.28	10.76	11.06
21	Deduction of profits of	31.37	34.85	14.84	15.26
23	industrial undertakings derived from integrated business of handling , storage and transportation of	1.69	1.88	0.52	0.53

24	Deduction of profits of undertakings engaged in	26.93	29.92	183.29	188.49
	developing and building housing				
25	projects (Sec 80-IBA)	1,886.52	2,095.90	1,202.15	1,236.29
25	Deduction of profits of undertakings setup in Sikkim (Sec 80-	2,094.08	2,326.50	2,031.33	2,089.02
28	IC)	645.36	716.99	331.26	340.66
26	Deduction of profits undertakings set up in North	804.72	894.04	1,239.84	1,275.05
29	Deduction from Business of Collecting and processing of bio degradable waste (Sec 80-JJA)	43.25	48.05	13.79	14.18
30	Deduction in new workmen (Sec 80-JJAA)	294.71	327.42	1,274.09	1,310.27
31	Deduction in respect of certain incomes of OBUs &IFSC (Sec 80-LA)	69.04	76.70	352.02	362.02

32	Deduction of hotelsconvention centresin specified areas (Sec 80-ID)	0.90	1.00		
Total		1,30,184.41	1,33,953.59	1,20,564.67	1,23,988.7

Revenue impact of major tax incentives for corporate taxpayers during financial years 2016-17, 2017-18, 2018-19 & 2019-20.

S. No.	Nature of Incentives	Revenue impact (in Rs crore) [2016-17]	Projected Revenue Impact (in Rs crore) [2017-18]	Revenue impact (in Rs crore) [2018-19]	Projected Revenue Impact (in Rs crore) [2019-20]
1	Deduction of export profits of units located in SEZs (Sec 10AA)	360.59	461.70	740.15	761.17
2	Accelerated Depreciation (Sec 32)	1,278.66	1,440.73	744.84	765.99
3	Deduction/weighted deduction for expenditure on scientific research (Sec 35 (1),(2AA)&(2AB))	8.22	9.27	8.56	8.80
4	Deduction for expenditure on eligible projects or schemes for the social and economic uplift of the public (Sec35AC)	10.57			
5	Deduction in specified business(Sec35AD)	57.61	73.76	48.58	49.94
6	Deduction on donations to	93.12	119.23	111.74	114.91

	charitable trusts and institutions (Sec 80G)				
7	Deduction on account of contributions to political parties (Sec 80GGC)	5.57	7.13	39.71	40.84
8	Deduction of profits of undertakings engaged in development of infrastructure facilities (Sec 80-IA)	118.97	152.33	235.07	241.75
9	Deduction of profits of undertakings engaged in development of SEZs and Industrial parks (Sec 80-IA)	12.60	16.14	22.24	22.87
10	Deduction of undertakings engaged in providing telecommunication services (Sec80-IA)	0.93	1.20		
11	Deduction of undertakings engaged in generation transmission and distribution of power (Sec 80-IA)	262.18	335.69	836.88	860.64
12	Deduction ofundertaking engaged in revival of power plant (Sec 80-IA)	2.89	3.70	3.92	4.03

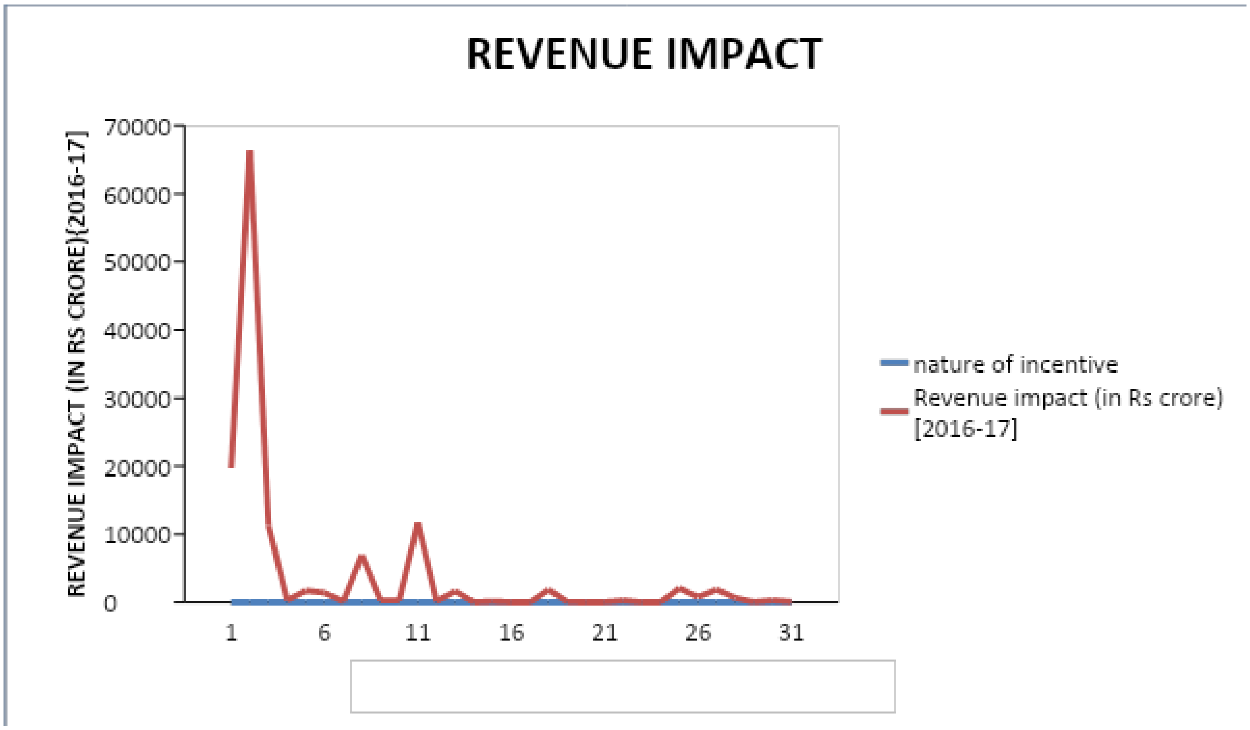
13	Deduction of undertakings engaged in development of	30.56	39.12	44.97	46.25
	SEZs in pursuance to SEZ Act ,2005 (Sec 80-IAB)				
14	Deduction due to undertakings located in Jammu & Kashmir (Sec 80-IB)	14.54	18.62	5.28	5.42
15	Deduction due to undertakings located in industrially backward states other than Jammu & Kashmir(Sec 80-IB)	0.14	0.18	0.02	0.02
16	Deduction of undertakings located in backward districts (Sec 80-IB)	0.56	0.71	0.01	0.01
17	Deduction of undertakings derived from Housing projects (Sec 80-IB)	89.92	115.14	56.04	57.63
18	Deduction of operating cold chain facility (Sec 80-IB)	4.19	5.36	3.03	3.11
19	Deduction from integrated business of handling storage and transportation of food grains (Sec	2.18	2.80	6.13	6.30

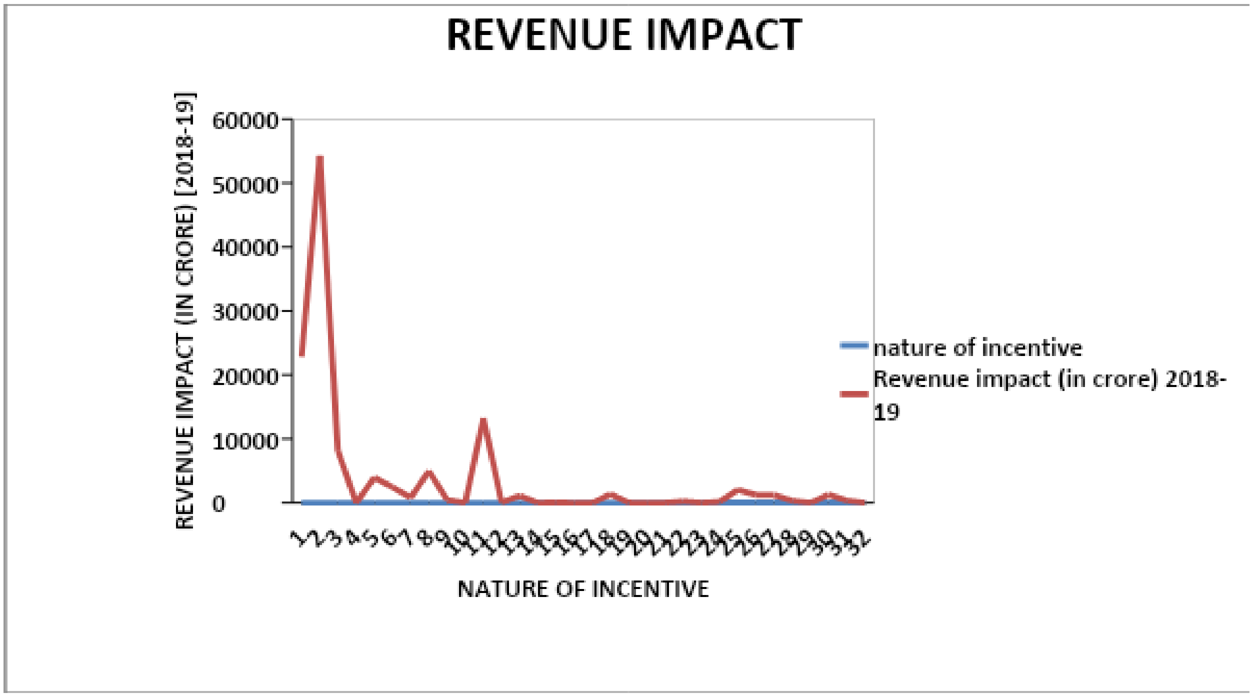
	80-IB)				

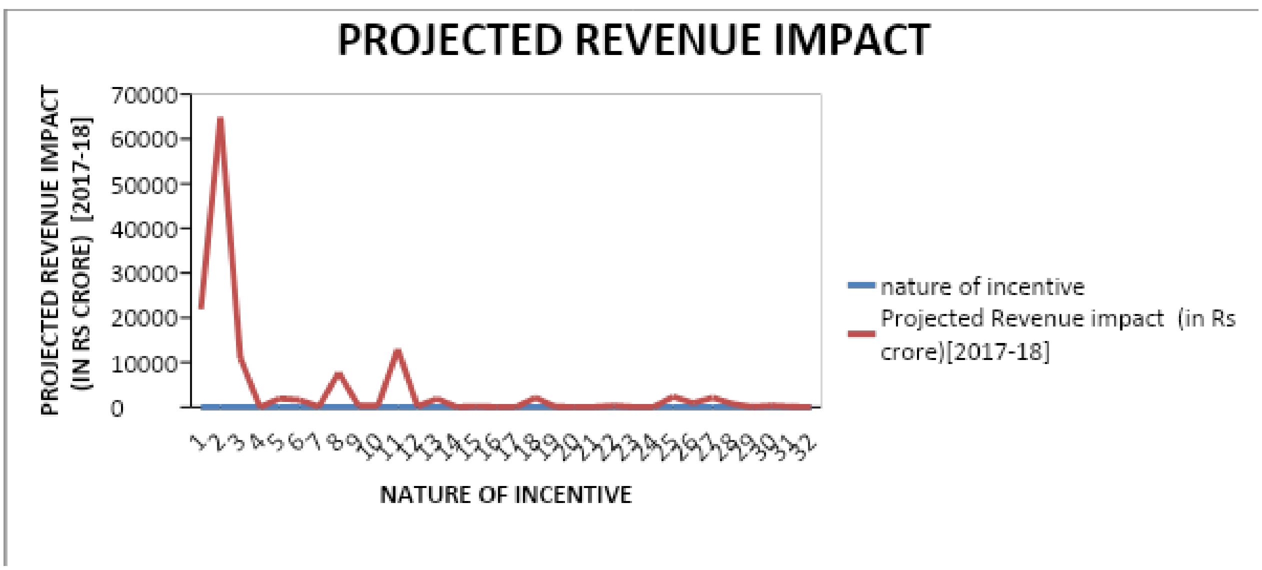
20	Deduction that come with undertakings derived from processing preservation and packaging of fruits and vegetables (Sec 80-IB)	20.61	26.38	25.97	26.70
21	Deduction that come with undertakings engaged developing and building housing projects (Sec80-IBA)	1.15	1.47	124.17	127.69
22	Deduction that come with undertakingsset-up in North Eastern States (Sec 80-IC)	98.57	126.21	229.69	236.21
23	Deduction that comewith undertaking set up in Sikkim (Sec 80-IC)	37.88	48.50	44.77	46.04
24	Deduction that come with undertakingsset-up Uttarakhand (Sec 80-IC)	95.49	122.26	63.27	65.06

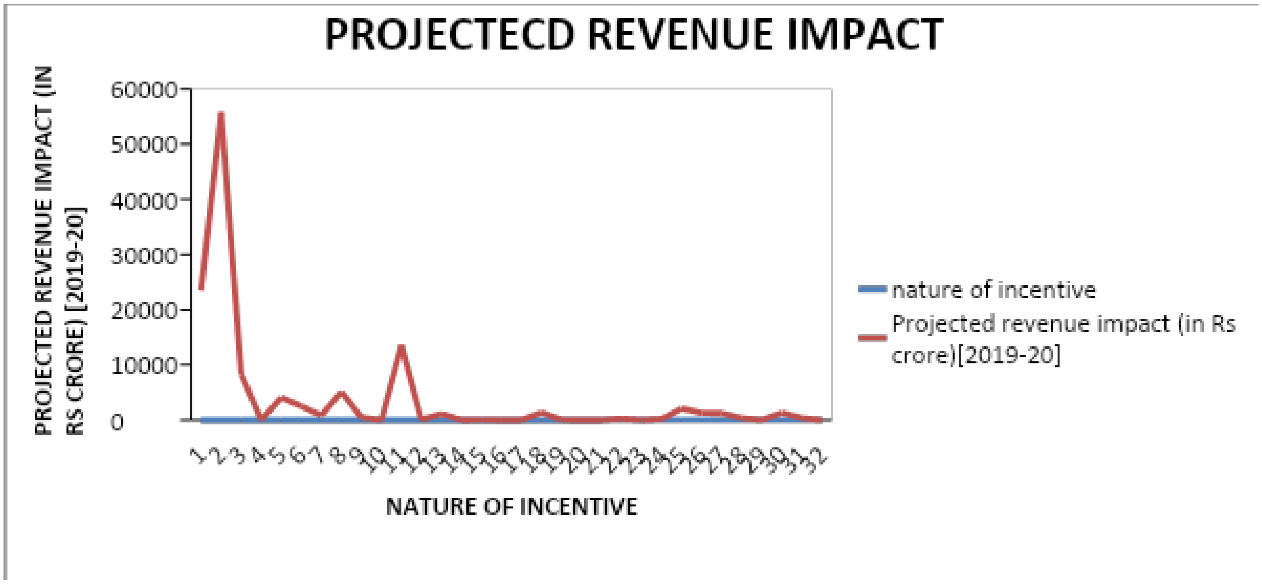
25	Deduction that come with undertakings set-up in Himachal Pradesh (Sec 80-IC)	138.50	177.34	103.53	106.47
26	Deduction of profits from collecting business and related to bio-degradable waste (Sec 80JJA)	4.20	5.38	10.01	10.29
27	Deduction of certain incomes of OBUs &IFSC (Sec 80-LA)	5.95	7.62	1.13	1.16
28	Deduction in respect of hotels, convention centres in specified area (Sec 80-ID)	0.52	0.67		
29	Deduction in profits of cooperative societies (Sec 80P)	2,090.40	2,676.56	3,493.69	3,592.91
Total		4,847.28	5,995.22	7,003.38	7,202.27

Revenue impact of major tax incentives for non- corporate (Firms / AOPs /BOIs) taxpayersduring the financial years 2016-17, 2017-18, 2018-19 & 2019-20.

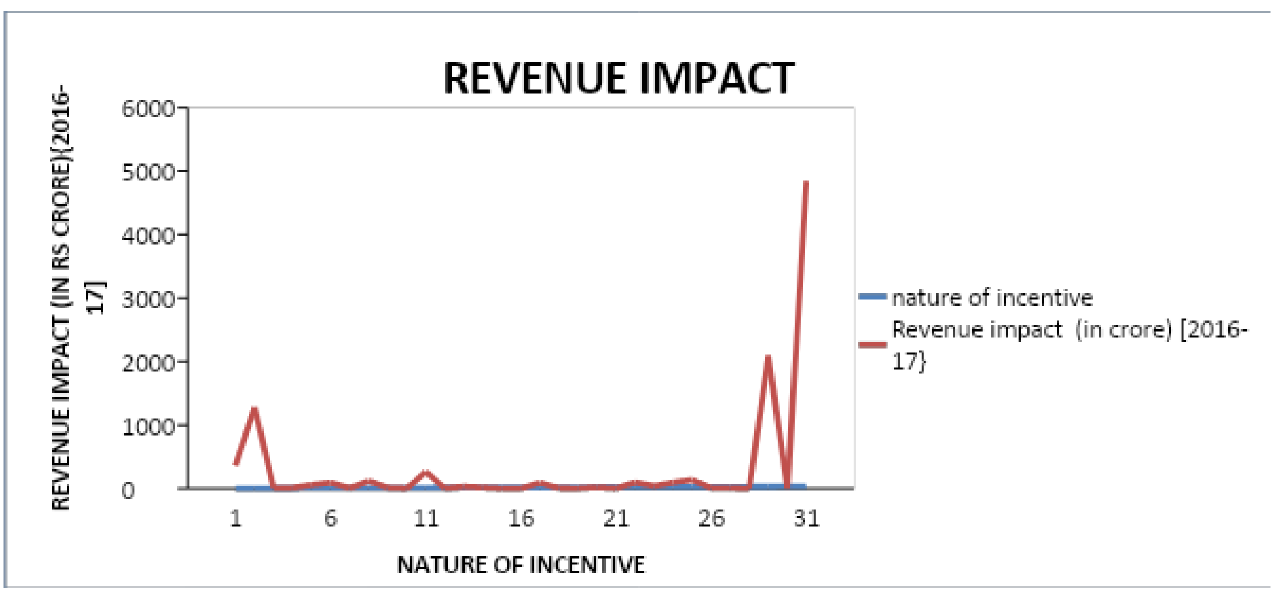


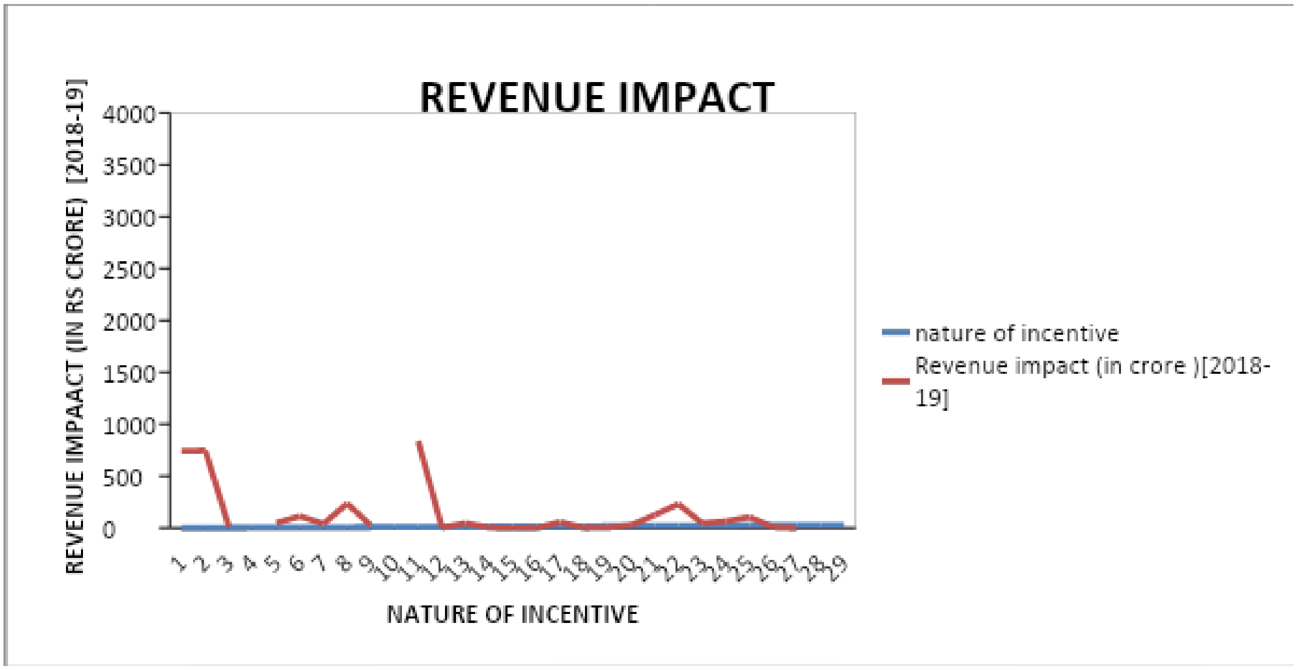

REVENUE IMPACT
REVENUE IMPACT (IN CRORE) [2018-19]
60000
50000
40000
30000
20000
10000
0
NATURE OF INCENTIVE
nature of incentive
Revenue impact (in crore) 2018-19

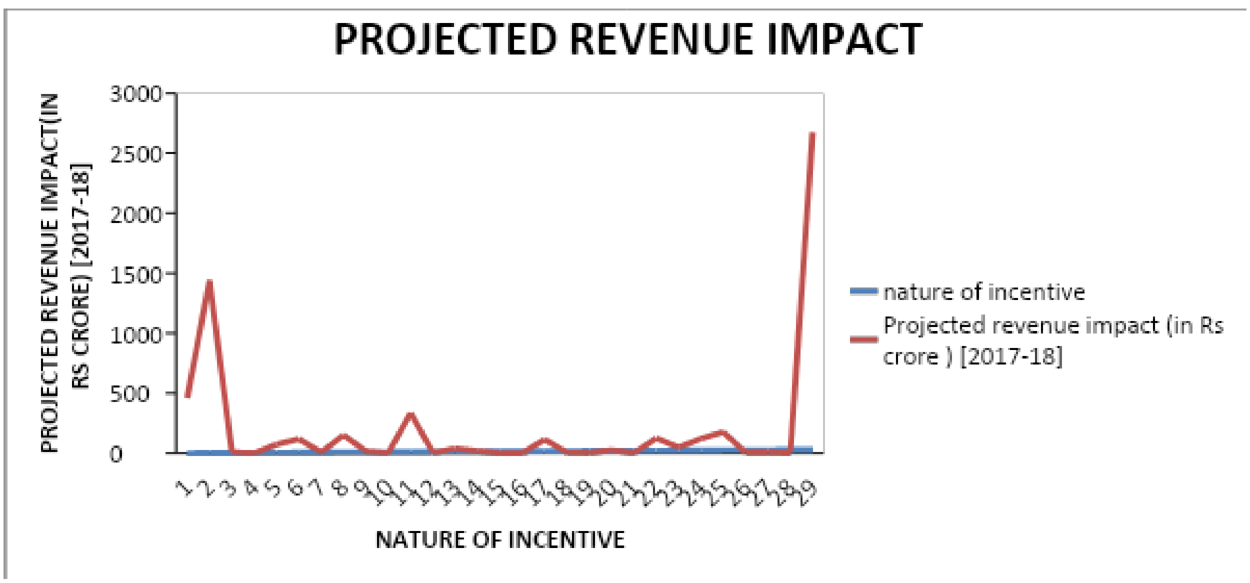

PROJECTED REVENUE IMPACT
PROJECTED REVENUE IMPACT (IN RS CRORE) [2017-18]
70000
60000
50000
40000
30000
20000
10000
0
NATURE OF INCENTIVE
nature of incentive
Projected Revenue impact (in Rs crore)[2017-18]

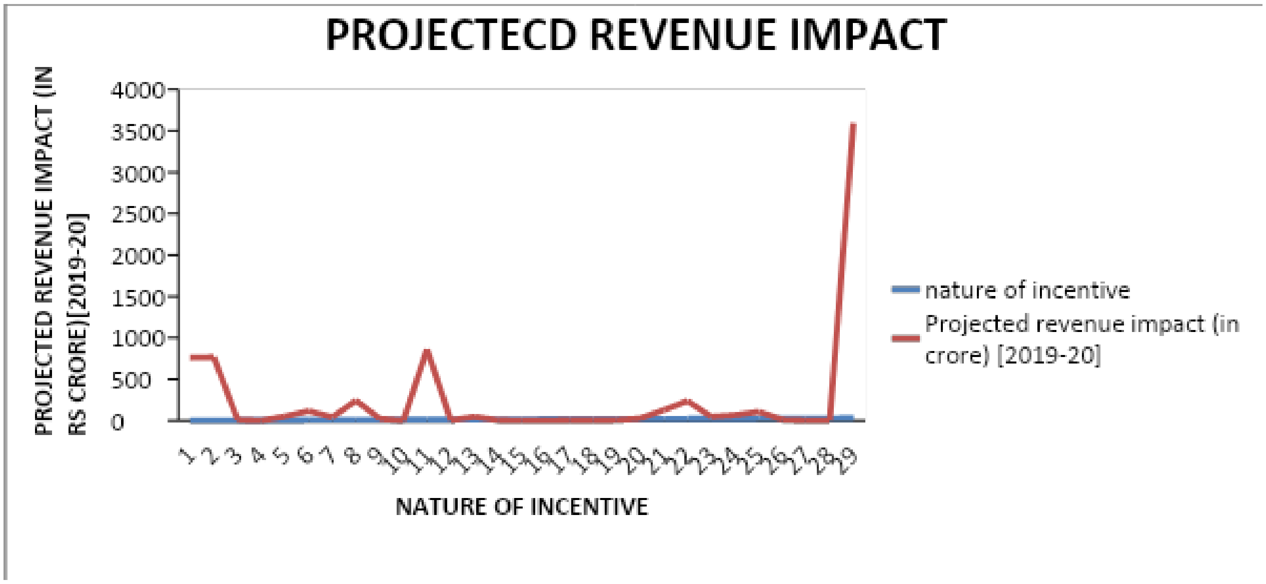


NON CORPORATE:-




REVENUE IMPACT
REVENUE IMPAACT (IN RS CRORE) [2018-19]
4000
3500
3000
2500
2000
1500
1000
500
0
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29
NATURE OF INCENTIVE
nature of incentive
Revenue impact (in crore)[2018-19]


PROJECTED REVENUE IMPACT
PROJECTED REVENUE IMPACT(IN RS CRORE) [2017-18]
3000
2500
2000
1500
1000
500
0
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29
NATURE OF INCENTIVE
nature of incentive
Projected revenue impact (in Rs crore) [2017-18]



Corporate sector :-

The above data shows the revenue impact of major tax incentives for corporate tax payers during the financial years 2016-17, 2017-18, 2018-19 and 2019-20. The highest amount of revenue impact is of accelerated depreciation with the value of Rs 66350.44(in crore) in 2016-17.However the value decreased to Rs 54278.39 in the year 2018-19. Deduction of export profits of units located in SEZs takes the next place in the picture with the revenue impact of Rs 19695.99(in crore) in 2016-17following with increase in revenue impact and projected impact in the next three financial year which stood Rs 21,882.02, Rs 22,889.65 and Rs23,539.72(in crore) respectively.

The lowest amount of revenue impact is of deduction of profits of eligible start-up accounting Rs 0.26crore in 2016-17 while that of deduction of profit of industrial undertaking located in drawback district is Rs 0.87crore being the second lowest among all. The deduction in respect of specified business, deduction on account of donations to charitable trust and institutions, deduction on account of contributions to political parties, deduction of profits undertakings engaged in generation transmission and distribution of power follow the same trend of increasingrevenue impact as well as projected revenue impact in all the subsequent years. It is also evident from the data that the deduction in respect of certain incomes of OBUs and IIFC has shown the largest fluctuation of increase in revenue impact from Rs 69.04 crore to Rs352.02 crore in the year 2016-17and 2018-19 respectively. Similarly with projected revenue impact which increased to Rs 362.02 crore in 2019-20 from Rs 76.70 crore in 2017-18.

Non-corporate :-

Taking into the consideration the revenue impact of major tax incentives for non-corporate tax payers for the financial year 2016-17, 2017-18, 2018-19, 2019-20. The deduction in the respective for profits of corporative societies stood at the highest value of Rs 2090.40 revenue impact in year 2016-17 which increased further to Rs 3493.69 crore in 2018-19 similarly with projected revenue impact which increased to Rs 3493.69 crore in 2018-19 from Rs 2676.56 in year 2017-18.

It is then followed by accelerated depreciation which decreased from Rs 1278.66 crore in 2016-17 to Rs 744.84 crore. The revenue impact of deducted/ weighted deduction for expenditure on scientific research increased from Rs 8.22 crore in 2016-17 to Rs 8.56 crore in 2018-19 while projected revenue impact decreased from 2017-18 to 2019-20. Deduction on account of donations to charitable trusts and institutions, deductions on account of contributions to political parties deduction of profits of undertaking whose revenue impact decreased from 2016-17 to 2018-19. The total of revenue impact increased from Rs 4847.28 crore to Rs 7003.38 crore in 2018-19 while that of projected revenue impact increased from Rs 599.22 crore to Rs 7202.27 crore.

Chapter 4

ANALYSIS

Through the proper analysis of data it is clear and evident that government provides lots of incentives to the corporate as well as non-corporate sectors in the form of deductions and exemptions .Some of the nature of tax incentives are broadly classified in the data along with the revenue generated from such incentives. Working on this paper, I have found that some tax incentives are fruitful to the government but some are not very desirable and efficient from economic point of view.

Talking the corporate sector first, there are various tax incentives which has generated sufficient revenue in the year 2016-17 and 2018-19 and are found quite legitimate to be there in

the incentives list such as accelerated depreciation (Sec 32), deduction for expenditure on scientific research (Sec 35 (1),(2AA)&(2AB)), deduction of export profits of units located in SEZs (Sec 10AA) but on the other side there are various tax incentives which have not generated sufficient revenue impact and are doubtful such as deduction of profits of undertakings engaged in providing telecommunication services (Sec 80-IA)

Similarly if we talk about the incentives provided to the non-corporate sector, again on the top ofthe list is the accelerated depreciation as the highest revenue generating tax incentives followed by some other such as deduction of export profits of units located in SEZs (Sec10AA), deductionof profits of undertakings engaged in development of infrastructure facilities (Sec 80-IA), deduction of profits of undertakings engaged in generation transmission and distribution of power (Sec 80-IA), deduction in respect of profits of cooperative societies (Sec 80P) but considering the case of the tax incentives which are not generating sufficient revenue such as deduction of profits of industrial undertakings located in industrially backward states other than Jammu & Kashmir (Sec80-IB), deduction of profits of industrial undertakings located in backward districts. (Sec 80-IB), deduction of profits of industrial undertakings derived from operating a cold chain facility (Sec 80-IB).

Hence it can be said that tax incentives do generate sufficient revenue and also improves the deficit making it a good fit for the economy if provided virtuously. Moreover the tax incentives / tax expenditures are exogenous to the tax structure which clearly means that the government can add or delete tax incentives for mobilizing revenue and government should do the needful in the case of the incentives which are not practical or appropriate.

Hence our Alternative Hypothesis (H11) is accepted and proved that there is a significant relationship between tax incentives and GDP.

Chapter 5

CONCLUSION

There are few areas relating to existing literature on the relation of tax incentives and economic growth. The relationship between tax expenditure and the economic growth is not direct but rather deduction and exemptions related to tax incentives / tax expenditure help in generation of revenue which therefore leads to the economic growth.

This study has also tried to explain the same relation by taking various incentives provided by the government and then thereby studying the revenue generated from such incentives in both corporate and non-corporate sector and further analysing all the incentives properly it can be argued that not all the incentives are fruitful. Therefore there is need for reforms or furthersimplifications in this area as well.

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Receipt of Budget, 2018-2019, Annexure 7 Statement of Revenue Impact of Tax Incentives under the Central Tax System: Financial Years 2016-17 and 2017-18