

Classification of Taxes

A tax is a compulsory contribution by a public authority. A tax-payer does not get any direct service in return for the payments are called upon to make by the public authority. A tax can be classified according to the objectives; nature and the volume and on the basis of method.

(1) Single Vs Multiple tax system

A tax system comprising only one tax has been advocated at times in the past. Partly this was due to the inadequate understanding of the working of a complex modern economy, and partly it was the result of the belief in the concentration theory of incidence.

Single tax system

One single form of a single tax is the poll tax; which is imposed on a person simple because he is there in the society and not because we have an income, or wealth, or is following any particular trade or profession etc.

Multiple tax system

Since no single tax can be expected to help the economy on all fronts, a choice for a multiple tax system becomes inevitable. Multiple tax system can be justified as different taxes contribute to the attainment of different objectives. Thus some would help in the redistribution of income and wealth. More equally, others would help the economy in the direction of regional balanced growth.

(2) Proportional Vs progressive taxes

A common classification adopted is that on the basis of degree of progression of a tax. A tax is called progressive when with increasing income, the tax liability not only increases in absolute term but also as a proportion of the income. If on the other hand, the tax liability increases in the same proportion as the increase in income, then it is proportional taxation.

It can be called a regressive tax if the tax liability as a proportion of income, falls with increase in income. The absolute tax liability even in that case may increase. This can be better explained by the use of tax base. A tax base is the legal description of the objects to which the tax applies such as net income of an individual, the value of a property and so on. Accordingly, when the tax rate

remained unchanged for the tax base, it would be called proportional. If the rate rises as the tax base increase, we have progressive tax and the tax is regressive if the tax rate diminishes as the base increases.

(3) Direct Vs Indirect taxes

The distinction between direct and indirect taxes is not always a satisfactory or a consistent one. One way of distinguishing between these them has been in terms of the incidence of taxation. It is asserted that if the incidence of a tax rests upon the person who bears its impact also then it is a direct tax. On the other hand, the incidence is passed on to others, and then it is an indirect tax.

The economic basis for distribution between direct and indirect taxes, then the plausible approach would be to maintain that in the case of direct reference to the tax paying ability of the tax-payer. While in the case of indirect taxes such an ability is assessed indirectly in relation to the income is a true indicator of his tax paying ability.

Same is the case with gift tax, inheritance tax, expenditure tax, wealth tax and so on. All these are examples of direct taxes, corporation taxes, such as taxes on profits, sales proceeds of firms and corporation are also direct taxes. An excise duty, on the other hand, is an indirect tax. For example if each pieces of radio is taxed at rate of 20 per cent of its value, then it is assumed that a person who purchases a radio will have this capacity to pay the tax and one who purchases a costlier radio will have greater ability to pay. It is partly on the reasoning that costlier items and luxuries are usually subject to higher sales taxes or excise duties while necessary items are generally exempted or taxed lightly. Import-export duties, taxes on rail and so on are also in the category of indirect taxes.

Value-added tax

Value added tax (VAT) belongs to the family of sales tax. A general sales tax is a tax on sales transaction but it is applied at only one state of business activities right from the manufacturer to the retailer. Usually it is collected either at the whole sale level or at retail level. The trader is allotted sales tax members and a trader possessing such a number can purchase the goods without paying the sales tax. VAT is a tax not on the total value of the good being sold, but only on the value added to it by the last seller.
