THE TAXATION SYSTEM IN INDIA: EVOLUTION THROUGH THE LENS OF THE INDIAN KNOWLEDGE SYSTEM

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Abstract

The Indian Knowledge System (IKS) has profoundly influenced governance, economics, , business and trade and ethical frameworks within India's long civilizational history. This paper investigates the evolution of India's taxation system from ancient traditions to modern institutional reforms, contextualized through the ethical and philosophical lens of IKS. According to the primary sources such as the 'Arthashastra', 'Manusmriti', and other classical treatises, alongside modern fiscal policies and reform committee reports, the study identifies enduring continuities in fiscal ethics - fairness, accountability, and distributive justice. Through an analytical synthesis of historical evolution, colonial transformation, post-independence restructuring, and the incorporation of contemporary digital governance, the paper argues that IKS principles remain vital to fostering transparency and equity in modern fiscal administration. The present study intends to describe the sustainable taxation in India continues to derive legitimacy from its alignment with dharmic (religious) principles of justice and welfare.

Introduction

Taxation constitutes one of the most enduring pillars of governance, linking the moral economy of the state to its administrative apparatus. India's fiscal evolution is unique in its continuous dialogue between spiritual-ethical traditions and pragmatic statecraft. The Indian Knowledge System (IKS) - a composite of philosophical, administrative, and ethical insights provides a moral and intellectual foundation for understanding taxation as both a civic duty and a mechanism for redistributive justice. By drawing the transformation of taxation from early age through colonial codification and modern reforms, this study highlights the Indian fiscal governance as a continuum rooted in indigenous rationality yet adaptable to global exigencies.

India's tax system traces its roots to ancient texts, particularly Manusmriti and Arthashastra, which advocated equitable taxation, economic stability, and governance. Taxation historically supported state welfare and prevented excessive concentration of wealth. Today, these historical principles influence policies aimed at efficiency, equity, and inclusive growth. Tax revenue collection is at the core of public fund mobilization for various public expenditure programmes and is very popular source of revenue generation mechanism since ancient period. Taxation is the cheapest source of revenue mobilization since it is not *quid pro quo* i.e. nothing is payable by the government (tax collector) in consideration of tax revenue collection. As a result, the taxpayers become unhappy to forego their hard-earned money. Accordingly, it is well recommended that tax should be levied without harming the taxpayers as bees collect honey without harming the flowers.

The Foundations of Taxation in the Indian Knowledge System

Ultimately, India's knowledge and taxation systems represent a synthesis of ancient wisdom and modern advances, guiding both social development and fiscal management. India is an old country with a rich heritage. In India, the direct tax system as it is known today, has been in force in one form or another even from ancient times. There are references both in Manusmriti and Arthashastra to a variety of tax system. Classical Sanskrit sources systematically addressed the aims, principles, and mechanism of taxation. The Dharmashastra tradition (exemplified by Manusmriti) articulates a normative stance and the sovereign's right to levy contributions was justified by the duty of protection. The taxation was bounded by principles of moderation and equity. The recurring prescription of a one-sixth share for the sovereign in several Dharmashastra and Smriti passages indicates an early canonical benchmark for land and produce-based levies; commentators and comparative studies have interpreted this 'one-sixth' as both a moral and pragmatic rule that balanced state needs with agrarian sustainability. Manu advocated moderate taxation, so that the subjects are not hit hard by taxes. Taxes in those days, in Manu's time were imposed by the king on traders, artisians, dancers, actors, and singers etc. These texts also distinguish taxes from other dues (fines, gifts, and fees), which also recommend for remissions in times of calamity, and insist on administrative probity - features that anticipate later canonical tax principles. The tax structure was a broad based and it brought most of the people under its ambit.

Kautilya's 'Arthashastra' supplements the Dharmashastra prescriptions with a technocratic and pragmatic manual of statecraft. It classifies the sources of revenue (land, trade, customs, forestry, mining and state industries), prescribes proportionate methods of assessment, and emphasizes on regular accounting procedures, appointment of specialized officers, and use of local informants and inspectors for assessment and collection. The Arthashastra stipulates graded assessments based on soil fertility and productivity, allows remission during crop failure, and prescribes penalties and audit measures to prevent corruption. Collectively, 'Manusmriti' and 'Arthashastra' form a combined normative-technical corpus that shaped fiscal decision-making in early Indian polities.

Beyond procedural detail, the IKS puts the taxation within an ethical economy: revenue was conceived as a social contract rather than a unilateral extraction. The ruler's legitimacy rested on distributive outcomes—roads, irrigation, inns, and educational support—and the texts repeatedly link fiscal policy to public welfare. Kautilya argues that revenue must secure the state's longevity while not undermining the productive capacity of the populace; this produced rules such as variable rates based on land classification and exemptions during natural calamities. Such policies manifest early versions of what modern public finance terms as 'ability-to-pay' and 'ability-to-produce' principles

During the Gupta dynasty, emperor Chandragupta introduced tax on profit which is a form of levy tax on income. Kautilya in his famous treatise 'Arthasastra' dwelt in length on the financial system of Maurya Empire. The Maurya kings used to collect revenue from agricultural production. Taxes were also imposed on forest, mining and on export and import trade. The revenue so earned by the king was to be utilized for the protection of their subjects and for public welfare e.g. roads, educational institutions, inns on the road side, plantation and such other activities relating to the social welfare. According to Kautilya, revenue earned by the Sovereign, made the king responsible to return the same to the subjects in the form of welfare activities. The Arthashastra prescribes a range of non-tax revenue-generating activities (state monopolies, manufactories) to diversify the fiscal base, and both traditions emphasize record-keeping and audit to reduce corruption. Ethical injunctions - moderation, fairness, and the duty of the sovereign to return the yield in welfare constitute a fiscal ethic that complements technical rules and underpins the sustainability of taxation in the subcontinent. It is very interesting to learn from Kautilya's Arthasastra that, even in those days a judicious taxation system prevailed.

Theoretical Framework

Existing literature on taxation in India spans economic history, administrative theory, and comparative governance. Classical sources like Kautilya's 'Arthashastra' (Shamasastry, 1915) and 'Manusmriti' (Bühler, 1886) emphasize ethical taxation and fiscal responsibility as extensions of state dharma. Sarkar's (1978) seminal work 'Public Finance in Ancient India' found these prescriptions as precursors to modern fiscal accountability. The analyses made by Chelliah (1992), Kelkar (2002), and Shome (2012) focus on rationalization, efficiency, and compliance in post-independence reforms. Recent studies (NIPFP, 2019; CBDT, 2022) further highlight digitalization, indirect tax like Goods and Services Tax (GST) implementation, and ethical governance. This literature collectively underscores that IKS values of moderation, transparency, and welfare continue to resonate within India's fiscal discourse.

Historical Evolution of the Tax System

Ancient and Medieval Periods:

Ancient Indian taxation, codified in 'Manusmriti' and 'Arthashastra', combined ethical restraint with administrative precision. The king, according to Manu, was entitled to levy moderate percentage of agricultural produce - typically one-sixth ensuring state sustenance without exploitation. The Mauryan Empire institutionalized these practices through trained officials and record-keeping systems (Arthashastra, Book II). The king generally collected more revenue from his subjects. The traders had to pay lump sum donations to meet the cost of war. It would not be out of place to mention that the Indian Taxation Policy in many respect is similar to that of the Maurya era. We get some other terms in the history of ancient and medieval India like 'Rajaswa', 'Sardesh-mukh' etc. which were nothing but the various types of taxes levied by the kings of that time. Even there was instance of levy tax on 'religion'. Epigraphic and textual sources suggest systematic land revenue assessments tied to land quality and yield; some estimates and readings of the Arthashastra indicate shares ranging from one-sixth to one-fourth of produce depending on circumstances. Taxes on trade (tolls, tariffs), artisanal professions, and resource exploitation (forestry, mining) expanded the fiscal base and reflected a pluralistic revenue system.

During the Sultani period, Al-uddin Khilji had imposed 'Jakat' and 'Jijia kar' and later Mughal administrations introduced their own tax categories also incorporating pre-existing local practices. At the same time, mechanisms of remissions, local self-assessment in villages, and patronage-based exemptions persisted, underscoring continuity in administrative pragmatism. From all these evidences, it can be inferred that among different taxes which were prevalent in ancient and medieval times, income tax was an integral part of the taxation policy as the major source of revenue in the hands of the legislative authority/ government.

Colonial Reconfiguration:

The modern tax system in India was actually introduced by the 'British' when India was under the British rule. The history of the modern tax system in India began its journey in phased manner.

The colonial approach prioritized revenue extraction over welfare, diverging from IKS ethics of balance and equity. British colonial rule transformed indigenous fiscal systems through codification, centralization, and monetization of tax obligations. The first Income Tax Act (1860), introduced by Sir James Wilson to meet fiscal exigencies after the 1857 uprising (Sepoy Mutiny), represented a new legalistic approach - taxes were classified and organized under different heads, assessments were formalized. Subsequent legislative reforms (Income Tax Acts of 1869, 1886, 1918, and 1922) progressively refined definitions of income, created administrative institutions (e.g., the Central Board of Revenue, 1924), and separated procedural law from prescribing tax rate (delegating to the annual Finance Acts). While the colonial state introduced administrative rigour—standardized book-keeping, audit trails, and legal appeals—it also prioritized revenue extraction for imperial purposes, which in certain regions intensified burdens on producers. Although the colonial legacy left behind a comprehensive legal-fiscal framework, the post-colonial state inherited these framework and repurposed them in shifting their orientation towards developmental governance, equity, and inclusive growth in taxation. The government gave top priority to industrialization because it was argued that a strong industrial foundation would bring about economic freedom for all.

The Modern Era: Reform process

Post-independence India faced the dual challenge of sustaining welfare commitments and promoting economic growth. The Income Tax Act of 1961 became the bedrock of direct taxation, consolidating earlier statutes and empowering the Central Board of Direct Taxes (CBDT). Some of the reform committees viz. Nicholas Kaldor (1956), Mahavir Tyagi (1958), K. N. Wanchoo (1971), C.C. Chokshi (1977), Raj Chelliah (1991), Vijay Kelkar (2002), and Parthasarathi Shome (2013) played pivotal roles in restructuring fiscal administration, aligning it with global practices while emphasizing simplicity and equity. The Wanchoo Committee underscored the need to curb evasion through administrative vigilance, while the Chelliah Committee advocated for lower rates and a broad base to enhance compliance. Kelkar Committee later promoted digitization and self-assessment models, setting the stage for e-governance and transparency in tax administration.

Corporate taxation (business and trade) represents the intersection between fiscal policy and industrial development. Since independence, India has sought to balance revenue generation with investment promotion. Early frameworks granted incentives for industrialization in backward regions, reflecting distributive justice akin to the IKS notion of 'samabhava' (balance). Post-1991 liberalization, the corporate tax system underwent major restructuring to attract foreign investment and ensure global competitiveness. The reform exemplifies the shift toward efficiency and growth-oriented fiscal framework of the country. Tax incentives (in the form of allowances, deduction, and tax holidays), provided by the act for the infrastructure and export enterprises, reflect Kautilya's recommendation for state patronage of productive activities and removing the regional imbalances. Corporate Social Responsibility (CSR), mandated under the Companies Act of 2013, reintroduces an ethical dimension akin to ancient practices of social contribution ('dana' and 'seva'). The fiscal architecture thus integrates economic rationality with moral accountability, ensuring that corporate profits contribute to public welfare - a continuation of 'dharmic' fiscal principles of the ancient times.

The introduction of the Goods and Services Tax (GST, 2017) in India is the biggest economic reform in the post-independent era which has redefined the country's taxation landscape significantly. By promoting ease of living and ease of doing business, it has turned the vision of "One Nation, One Tax" into a reality. This reform embodies IKS principles of unity and rationality, simplifying compliance and reducing cascading effects.

Digital platforms like the Income Tax Portal and the introduction of online assessments have further operationalized ethical transparency. These changes signify a moral and administrative continuity - the ancient principle of fairness is now implemented through technological efficiency. Modern fiscal policy in India also embodies redistributive justice. Programs such as 'PM-KISAN', 'Make in India', 'Digital India' and targeted subsidies resonate with the ancient ethos of welfare-centric technology driven governance. In integrating fiscal rationality with social equity, India's taxation system continues to reflect its IKS heritage while adapting to global economic paradigms. India has implemented extensive digital initiatives to modernize its taxation system, aiming for greater efficiency, transparency, and compliance.

Integrating Indian Traditional Knowledge into Modern Fiscal Governance:

The relevance of IKS in contemporary fiscal governance lies in its holistic integration of ethics, administration, and sustainability. Ancient fiscal philosophy emphasized the symbiotic relationship between the ruler and the citizens, with taxation framed as a moral obligation rather than coercion. Modern fiscal policy, through participatory governance, social audits, and welfare budgeting, echoes this relational ethic. The IKS principle of 'Artha' - the rightful pursuit of material prosperity, requires balance with 'Dharma' (ethical conduct), providing a theoretical foundation for inclusive taxation.

Integrating IKS principles into fiscal management of the country involves three dimensions: transparency, proportionality, and welfare. India's digital tax reforms, data-driven compliance, and citizen-centric e-filing systems operationalize these ideals. Moreover, reforms in both the direct and indirect taxes and Direct Benefit Transfer (DBT) mechanisms embody the concept of equitable redistribution, minimizing corruption and enhancing accountability. The incorporation of sustainability indicators in budgetary processes also reflect the ecological sensitivity of traditional Indian economic thought. The traditional practice of governance as is found in the IKS envisions taxation as an ethical ecosystem that balances efficiency with empathy. Fiscal responsibility and social obligation are not merely administrative concerns but expressions of 'rajadharma' - the duty of governance toward collective welfare. Thus, contemporary tax reforms that emphasize transparency, progressivity, and inclusion represent a civilizational continuity rather than an estrangement. The extant Income Tax Act, 1961 has been rehabilitated by the introduction of Income Tax Act, 2025 to be implemented with effect from 1st April, 2026 to cope with the changing fiscal governance scenario in the pursuit of modern Indian knowledge system.

Conclusion

The study demonstrates that India's taxation system embodies a deep continuity between ancient ethical principles and modern fiscal frameworks. IKS contributed moral legitimacy, administrative logic, and welfare orientation to fiscal design. While colonial codification introduced legal uniformity, post-independence reforms reinstated ethical and developmental imperatives. Recent digitalization and simplification initiatives actualize the IKS ideals of fairness and transparency through contemporary means. The synthesis of ethical tradition and technological modernization represents India's distinctive contribution to global fiscal thought.

Taxation in India is not merely a financial instrument but a reflection of its civilizational philosophy of balanced governance. IKS provides an enduring framework where ethical duty and administrative rationality coalesce. Policymakers can draw upon IKS insights - moderation, distributive justice, and public accountability to enhance fiscal legitimacy. As India advances toward deeper digital integration and greater global interdependence, embedding its indigenous ethical principles into the fiscal framework will help in aligning the economic growth with social welfare and environmental sustainability. MA

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