

**Economics
Seminar
Series
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**SOUTH ASIAN UNIVERSITY
FACULTY OF ECONOMICS**

Seminar

OPTIMAL TAXATION IN A FEDERATION AND GST IN INDIA

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Date: September 14, 2018
(Friday)
Time: 2:30 p.m.
Venue: FSI Hall, Akbar Bhawan,
Satya Marg, Chanakyapuri, New Delhi

All are Welcome

ABSTRACT

Optimal tax models, starting from Ramsey (1927), are often studied using a single government. However, there are several countries which are federations and multiple level of governments have fiscal authority. In this paper we study a federation with several states and a central government. We ask what the optimal design of taxation is and find that optimally either states, or the center should impose a consumption tax, but not both. We then characterize two equilibria, one where both the central government and state governments impose tax and two, where only the center imposes tax rates. We find that in the first equilibrium, though states can potentially impose different tax rates, consumption across states are the same, as is the case in the second equilibrium. However, aggregate consumption in the country is greater in the second equilibrium, when only the center imposes tax. We then calibrate the model to Indian data and find the revenue neutral tax rates. We find that the highest revenue neutral tax rate is 20.1% and the median rate is 11.4%. Using the calibrated indirect tax rates in a regression analysis, we find that tax rates at the state level is negatively related to the growth rate of the state. So, after the implementation of GST in India, some states may see a higher level of consumption tax rate in the state and hence, a fall in growth rate.