

Introduction to Taxation

Introduction to Taxation – Study Notes

1. What Is Taxation?

Aspect	Description
Definition	Compulsory financial charge imposed by a government on individuals, businesses, or transactions to fund public services and programs. • Raise revenue for government operations • Redistribute wealth (equity)
Purpose	• Influence economic behavior (e.g., encourage investment, discourage pollution) • Provide public goods (infrastructure, education, health). • Legally enforceable
Characteristics	• Non-voluntary (cannot be refused) • Collected by a sovereign authority • Varies by jurisdiction (national, state/provincial, local).

2. Core Principles of Tax Systems

Principle	Explanation
Equity	• Horizontal equity – taxpayers with similar ability to pay should owe similar taxes. • Vertical equity – taxpayers with greater ability to pay should owe more (progressivity).
Efficiency	Taxes should distort economic decisions as little as possible (e.g., low compliance costs, minimal impact on market prices).
Certainty	Tax laws must be clear, predictable, and applied uniformly.
Convenience	Tax collection should be simple for both the payer and the authority (e.g., withholding, electronic filing).
Economy	Administrative costs of tax collection should be low relative to revenue generated.

3. Main Types of Taxes

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Category	Sub?type	Typical Base	Example
Direct Taxes	• Income tax (personal, corporate)	Tax is levied directly on the taxpayer's income, assets, or net worth.	Personal income tax on wages; corporate tax on profits.
	• Property tax		
	• Wealth tax		
Indirect Taxes	• Sales tax / VAT	Tax is levied on transactions, goods, or services; the burden can be shifted to consumers.	10?% VAT on retail sales; gasoline excise tax.
	• Excise duties		
	• Customs tariffs		
Other Taxes	• Payroll/Pay?as?you?go (social security)	Specific events or transfers trigger tax liability.	Tax on profit from sale of stocks; tax on transferred estate value.
	• Capital gains tax		
	• Estate/inheritance tax		

4. Key Concepts & Terminology

Term	Meaning
Tax Base	The amount or value subject to taxation (e.g., taxable income, assessed property value).
Tax Rate	Percentage applied to the tax base (flat, progressive, or regressive).
Tax Credit	Direct reduction of tax liability (e.g., child tax credit).
Tax Deduction	Reduces taxable income before the tax rate is applied (e.g., mortgage interest).
Withholding	Pre?payment of tax on wages, collected by the employer and remitted to the tax authority.
Tax Gap	Difference between taxes owed and taxes actually collected (due to evasion, avoidance, or errors).
Tax Incidence	The ultimate economic burden of a tax—who really pays it (consumers vs. producers).

5. Tax Administration Process

1. **Legislation** – Parliament or legislative body enacts tax laws.
2. **Assessment** – Tax authority determines each taxpayer's liability (self?assessment or audit).

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3. Collection –