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Working Paper

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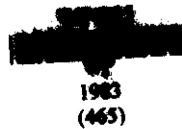
FISCAL POLICY AND THE POOR: MILES TO GO

By

ANAND P. GUPTA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FISCAL POLICY AND THE POOR

MILES TO GO

by

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I. POVERTY IN INDIA

A poor person is one who does not have command over or access to the basic needs of life. On the material plane, basic needs are fundamental physical needs like adequate food, drinking water, clothing and shelter which are necessary to stay alive and maintain working capacity. On the non-material plane are basic social services like education and health. The symptoms of poverty or the signs indicating lack of access to the basic needs are malnutrition, illiteracy, slum housing condition, inaccessibility of public facilities, high infant mortality and the like.

No single symptom can be relied upon for getting a realistic idea of the true incidence of poverty. This is because while a person may not be suffering from malnutrition, he may be illiterate. Similarly, a person may be literate, but he may be suffering from malnutrition. Further, the incidence of infant mortality in an area may not be high, but the people may be starving or skipping meals.

The picture of poverty in India differs from one part of the country to another. Take, for instance, poverty measured in terms of intake of calories. Table 1 presents state-wise data on daily calorie intake per capita, daily calorie requirement per capita, poverty line corresponding to the calorie requirement, and the percentage of people below the poverty

TABLE 1

INCIDENCE OF POVERTY IN INDIA

	Daily calorie intake per capita			Daily calorie requirement per capita		Poverty line (Rs.)		Percentage of people below poverty line	
	Rural	Urban	Rural urban combined	Rural	Urban	Rural	Urban	Rural	Urban
1	2	3	4	5	6	7	8	9	10
Andhra Pradesh	2209	2121	2192	2531	2140	60.13	58.05	70.2	47.6
Assam	2105	2031	2098	2238	2085	52.53	68.22	47.4	54.9
Bihar	2186	2300	2197	2411	2177	60.48	61.48	59.5	46.1
Gujarat	2180	2230	2194	2482	2107	55.25	68.97	52.3	52.5
Haryana	2971	2244	2843	2387	2095	50.64	63.39	28.1	46.7
Himachal Pradesh	NA	NA	NA	2529	2189	61.71	66.88	37.3	25.7
Jammu & Kashmir	2742	2497	2696	2417	2088	38.52	40.55	18.5	19.9
Karnataka	2211	1995	2158	2490	2135	59.91	70.12	66.5	59.0
Kerala	1534	1760	1571	NA	NA	NA	NA	NA	NA
Madhya Pradesh	2422	2108	2373	2527	2107	48.43	56.48	53.4	41.6
Maharashtra	2044	2163	2081	2531	2146	72.77	87.55	76.3	62.3
Manipur	NA	NA	NA	2276	2055	46.37	50.97	31.8	21.3
Meghalaya	NA	NA	NA	NA	NA	NA	NA	NA	NA
Nagaland	NA	NA	NA	NA	NA	NA	NA	NA	NA
Orissa	2125	2164	2128	2453	2123	50.33	53.39	65.6	44.3
Punjab	2818	2355	2708	2388	2105	53.41	61.60	25.2	34.0
Rajasthan	2719	2243	2635	2532	2095	50.56	55.97	34.8	38.1
Sikkim	NA	NA	NA	NA	NA	NA	NA	NA	NA
Tamil Nadu	2012	2091	2036	2557	2144	68.73	78.92	78.9	71.7
Tripura	NA	NA	NA	2359	2061	60.77	67.66	68.2	38.1
Uttar Pradesh	2450	2046	2393	2437	2080	47.01	50.31	46.4	39.7
West Bengal	2070	2196	2101	2311	2131	62.34	82.08	75.1	58.6
All India	2328	2003	2263	2435	2095	49.09	56.64	47.6	40.7

NA = Not Available

Sources: For columns 2-4: S. Sengupta and P.D. Joshi: "Consumption of cereals and energy content of food consumed", in Sarvekshana (New Delhi, NSSO), July 1978, p. 5.

For columns 5-10: K.L. Datta: "Measurement of poverty in India - statewise estimates", paper presented at the conference on social science research and the problem of poverty, Indian Association of Social Science Institutions, New Delhi, January 12-15, 1981, pp. 25-26.

line. The data, which relate to 1973-74, suffer from certain limitations. For instance, while the data on daily calorie requirement do take into account the inter-state differences in age-sex-occupation structure of the population, they do not take into account differences in, say, body weight and height of the people and climate. Further, the average per capita daily calorie requirement has been estimated on the basis of age-sex-occupation specific calorie allowances recommended in 1968 by the Nutrition Expert Group of the Indian Council of Medical Research. It has been argued that the per capita daily calorie requirement so estimated is appreciably higher than the minimum required for biological subsistence.[1] There are some other limitations. But we believe that the data presented in table 1 are the best data available today on the incidence of poverty in India's different states.

A striking feature of the data presented in table 1 is the magnitude of poverty in India. The incidence of poverty, measured in terms of inadequacy of daily calorie intake, is such that as much as 47.6 per cent of the people in the rural areas and 40.7 per cent of those in the urban areas lived below the poverty line in 1973-74. Available evidence does not suggest

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[1]See Government of India, Planning Commission, Perspective Planning Division: Report of the task force on projections of minimum needs and effective consumption demand (New Delhi, 1979), p. 7.

any perceptible decline in the incidence of poverty since 1973-74.[1] So if one goes by the population estimate revealed by the 1981 census, one can say that over 300 million people in India live below the poverty line.

One notices considerable inter-state differences in the incidence of poverty. There are nine states in which the incidence of poverty, both in rural and urban areas, is higher than the national average. These states are: Andhra Pradesh, Bihar, Gujarat, Karnataka, Madhya Pradesh, Maharashtra, Orissa, Tamil Nadu and West Bengal.

The states in which the incidence of poverty is higher than the national average, are not necessarily worse off in terms of per capita income. Take, for instance, the case of Maharashtra. According to the latest available data, this state has a per capita income of Rs. 1628[2] which is as much as 40 per cent higher than the national average.[3] One reason why the incidence of poverty in Maharashtra is higher than the national average is

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[1] A careful look at the Planning Commission data shows that while the all-India incidence of poverty declined from 51.49 per cent in 1972-73 to 48.13 per cent in 1977-78, it rose to 48.44 per cent in 1979-80. See Government of India, Planning Commission, Sixth Five Year Plan 1980-85 (New Delhi, 1981), pp. 51-52.

[2] Relates to 1977-78.

[3] The per capita consumption expenditure in Maharashtra is also higher than the national average.

that the poverty lines of this state happen to be much higher than the national averages. The poverty lines are high because (a) the per capita daily calorie requirements in Maharashtra are higher than the national averages (this is due to the particular age-sex-occupation composition of the population in the state), and (b) the yield of calories per rupee of consumption expenditure in Maharashtra is appreciably lower than the national average.[1]

A careful look at the data in table 1 reveals that a good part of the inter-state differences in the incidence of poverty may be due to inter-state differences in the yield of calories per rupee of consumption expenditure. Take, for instance, the case of Rajasthan and Tamil Nadu. One does not see much difference in the calorie norms of these states, but the poverty lines corresponding to their calorie norms differ quite a bit: the poverty lines for rural and urban Tamil Nadu are, respectively, 36 per cent and 41 per cent higher than those for rural and urban Rajasthan. If the yield of calories per rupee of consumption expenditure in Tamil Nadu were the same as in Rajasthan, the poverty lines for rural and urban Tamil Nadu would have been, respectively, 25.7 per cent and 27.4 per cent lower than those

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[1] The yield of calories per rupee of consumption expenditure may differ from one state to another due to (a) differences in the food habits of people, and/or (b) differences in the prices people pay for the goods they buy.

indicated in table 1. In that case the incidence of poverty in Tamil Nadu would certainly have been of a lower order.[1]

The incidence of poverty in a state may differ from region to region and in a region from season to season. Take, for instance, the case of Gujarat. A good look at the available data suggests substantial variations in the incidence of poverty within this state. According to a study conducted by the Government of Gujarat's Bureau of Economics and Statistics, the incidence of poverty in Gujarat is the highest (75.75 per cent) in the eastern hilly areas and the lowest (32.11 per cent) in the Saurashtra region.[2] Available evidence also suggests considerable season-to-season variations in the incidence of poverty. The Indian Institute of Management, Ahmedabad has recently completed a survey the results of which throw light on the incidence of poverty in the hilly region of Gujarat's Dharampur taluka.[3] According to this survey, in about 22 per cent of the sample households in the hilly region of this taluka, on an average,

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[1]Inter-state differences in the yield of calories per rupee of consumption expenditure are only one of the factors which may explain inter-state variations in the incidence of poverty. Other factors which may explain such variations are inter-state differences in per capita consumption expenditure and those in inequality in the distribution of consumption expenditures.

[2]Government of Gujarat, Bureau of Economics and Statistics: Incidence of poverty in Gujarat (Gandhinagar (Gujarat), Government of Gujarat, General Administration Department (Planning), 1973).

[3]T.K. Moulik, et al.: Dharampur block level plan (Ahmedabad, Indian Institute of Management, 1980).

an individual is forced to starve for 15 days in a year. The incidence of starvation starts in March and gets aggravated by July; it is the highest in September.

Having said all this, the question which arises is: How to deal with the problem of poverty in India? As we see things, the problem of poverty in India is such that it calls for action on many fronts, of which fiscal policy is one. The sections that follow take a good look at taxes and government expenditures in India and provide an idea of the role which fiscal policy can play in dealing with the problem of poverty in the country.

II. TAXES AND THE POOR

Taxation represents the largest single source of public revenues in India, accounting for over 80 per cent of the total revenue receipts of the centre, states and union territories. The taxes presently levied by the centre, states and union territories are: income tax, corporation tax, surtax, interest tax, wealth tax, gift tax, estate duty, stamp duty and registration fee, import duty, export duty, central excise duty, state excise duty, land revenue, agricultural income tax, central sales tax, state sales tax, tax on vehicles, taxes on passengers and goods, entertainment tax, tax on professions, calling and employment, etc. In addition, taxes (e.g., octroi duty, property

tax) are levied by thousands of local authorities spread all over the country.

The revenues of the centre, states and union territories have increased considerably over the last three decades - from Rs. 6,266.7 million in 1950-51 to Rs. 13,504.1 million in 1960-61, Rs. 47,524.1 million in 1970-71 and Rs. 198,437.5 million in 1980-81. It is estimated that tax revenues of the centre, states and union territories amounted to Rs. 240,269.2 million in 1981-82 and Rs. 272,284.5 million in 1982-83. And there is reason to believe that the figure would rise to about Rs. 314,000 million in 1983-84.

Viewed in relation to growth in national income, the tax revenues of the centre, states and union territories have recorded a fairly impressive performance. The percentage increase in tax revenues has been substantially higher than the growth in national income. The proportion of national income which the central government and the various state and union territory governments have been able (or have thought fit) to divert to the public sector through taxation, has moved up from 7.1 per cent in 1950-51 to 10.2 per cent in 1960-61, 13.9 per cent in 1970-71, 18.8 per cent in 1980-81 and 21.4 per cent in 1982-83. This is a fairly impressive achievement. Further, India's performance on the tax front compares favourably with other countries: While per capita income-wise India ranks 67th (among

84 countries for which relevant data are available), in terms of tax revenue as per cent of national income, the country ranks 57th.

The increase in tax revenue that has taken place over the last three decades, is not evenly distributed over the various taxes. Indeed, a careful look at the relevant data shows that a change amounting almost to a revolution has taken place in the proportions borne by the different taxes to the total tax revenues. Thus, income tax which contributed 21.37 per cent to the total tax revenues at the commencement of economic planning in India, now contributes only about seven per cent. Similarly, land revenue which contributed 8.23 per cent in 1950-51, now contributes less than one per cent.

On the other hand, revenues from central excise duty and sales tax have grown from only about one-fifth in 1950-51 to well over one-half now. This has been possible partly as a result of growth in production and consumption in the country, and partly as a result of deliberate policy efforts to make central excise duty and sales tax increasingly more intensive and more extensive.

DISTRIBUTION OF TAX BURDEN

Many attempts have been made over the last three decades or so to estimate the distribution of tax burden in

India. The first attempt was made by the Taxation Enquiry Commission which was appointed by the Government of India in 1953 under the chairmanship of John Matthai.[1] The Commission, which confined its analysis to formal incidence of taxes, selected income and residence (by rural and urban areas) as the main bases of its analysis. As data on income distribution were not available, the Commission used the household consumer expenditure data collected during the fourth round of the National Sample Survey (NSS). This was done on the assumption that expenditure approximately equalled income.[2]

The NSS data used by the Commission were collected during the period April-October 1952 and, therefore, pertained to the fiscal year 1952-53. They were, however, assumed to hold good for the fiscal year 1953-54, the year for which the Commission analysed the incidence of taxation. The taxes covered by the analysis were: central excise, import duties, opium excise, liquor excise, general sales tax, sales tax on

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[1] Government of India, Ministry of Finance, Department of Economic Affairs: Report of the Taxation Enquiry Commission 1953-54, Vol. I (Delhi, Manager of Publications, 1955), pp. 45-84.

[2] The Commission was aware of the limitations of this assumption but as no better data were available and as considerations of time and cost stood in its way of undertaking a comprehensive family budget inquiry designed specially for the purposes of a study of tax incidence, it was left with no alternative but to use the best of the data already available.

motor spirit, entertainment tax, inter-state transit duties, sugarcane cess, and motor vehicles tax.

The analysis of tax incidence for 1953-54 by the Taxation Enquiry Commission has been followed by two attempts by the Ministry of Finance, Government of India. These attempts have analysed incidence of indirect taxes for the fiscal years 1958-59[1] and 1963-64.[2] The concepts, coverage, assumptions and method of analysis were more or less the same as in the 1953-54 study by the Taxation Enquiry Commission, excepting one difference which may be noted. Unlike the 1953-54 study, these studies have taken consumer expenditure, and not income, as the base of their analyses and have, therefore, refrained from making the assumption of approximate equality between income and consumer expenditure.

Nearly seven years after the 1963-64 study was completed, the Government of India appointed, under the chairmanship of L K Jha, the Indirect Taxation Enquiry Committee to determine, among other things, the distribution of the burden of indirect

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[1]Government of India, Ministry of Finance, Department of Economic Affairs, Economic Division: Incidence of Indirect Taxation, 1958-59 (New Delhi, 1961).

[2]Government of India, Ministry of Finance, Department of Economic Affairs, Economic Division: Incidence of Indirect Taxation, 1963-64 (New Delhi, 1969).

taxes levied by the centre and the states among the different expenditure groups in rural and urban areas. The Committee entrusted this study to the National Institute of Public Finance and Policy, New Delhi. The Institute accordingly undertook a study which covered import duties, central excise duties, sales taxes, state excise on liquor, tax on passenger and goods, motor vehicles tax, entertainment tax, electricity duty and other taxes and duties. The study relates to 1973-74.[1]

The calculations carried out for 1973-74 for the Jha Committee have been extended to 1979-80 in a study undertaken by Ehtisham Ahmad and Nicholas Stern.[2] What Ahmad and Stern have done is that they have calculated the effective indirect tax rates on different commodities and have used these rates for calculating the proportion of tax in consumer expenditure for each household group.

In addition, a number of attempts have been made to estimate the distribution of tax burden in some individual states. The first such attempt was made by the Orissa Taxation Enquiry

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[1]Government of India, Ministry of Finance, Department of Revenue: Report of the Indirect Taxation Enquiry Committee, Part II (New Delhi, 1978), pp. 87-116.

[2]Ehtisham Ahmad and Nicholas Stern: Effective Taxes and Tax Reform in India, Discussion Paper Number 25 (Coventry, England, University of Warwick, Development Economics Research Centre, 1983).

Committee which was set up by the Government of Orissa in 1959 under the chairmanship of P S Lokanathan.[1] The Committee estimated the burden of taxes, both direct and indirect, on different income/consumption expenditure groups in the rural and urban areas. A state-wide family budget enquiry was conducted during February-April 1960 with a view to gather information for analysing the burden of taxation. The reference period was taken as one month for most of the items of consumption and a year for a few of them. Thus, data relating to consumption of cereals, milk and milk products, other food items, fuel and light, intoxicants, toilet and sundry goods were collected for a period of one month preceding the date of the survey, while for those relating to consumption of clothing, etc., miscellaneous goods and services, durable and semi-durable goods, the reference period was one year.

The direct taxes covered by the study were: land revenue, income tax, motor vehicles tax, radio license, cycle license, and other municipal, local rates and taxes. As regards indirect taxes, those which the Committee was able to cover in its study of tax incidence were: central excise duty on mill-made cotton clothing, sugar, tobacco, kerosene, matches, tea, coffee, leather footwear, cycles, and motor spirit; tax on

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[1] Government of Orissa, Finance Department: Orissa Taxation Enquiry Committee Report (1961), chapter IV.

railway fares; state sales tax on 50 items; purchase tax; state excise duty; entertainment tax; and motor vehicles tax.

The second attempt to estimate the distribution of tax burden at the state level in India was made by the Uttar Pradesh Taxation Enquiry Committee which was set up by the Government of Uttar Pradesh in 1968 under the chairmanship of J D Shukla.[1] The Committee, which selected household consumption expenditure and residence (by rural and urban areas) as the main bases of its analysis, confined its work on the distribution of tax burden to only the indirect taxes levied by the Government of Uttar Pradesh. The data on household consumption expenditure used by the Committee were those which were collected by the Directorate of Economics and Statistics, Uttar Pradesh, in collaboration with the Central Statistical Organisation of the Government of India. The data related to the period July 1965 to June 1966, but were assumed to hold good for the fiscal year 1965-66, the year for which the Committee analysed the distribution of tax burden. The taxes covered by the analysis were: sales tax, purchase tax on sugar cane, state excise duty, entertainment and betting tax, motor vehicle tax, sales tax on motor spirits, passengers and goods tax, and electricity duty. These taxes accounted for 63.94 per cent of the total taxes, amounting to Rs. 952.1 million, raised by the Government of Uttar Pradesh in 1965-66.

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[1] Government of Uttar Pradesh: Uttar Pradesh Taxation Enquiry Committee Report 1968-69 (Lucknow, 1969), chapter III.

The analysis of tax burden distribution for 1965-66 by the Shukla Committee has been followed by an analysis by the Taxation Enquiry Committee which was set up by the Government of Uttar Pradesh in 1974 under the chairmanship of D T Lakdawala.[1] Since it was not possible for the Committee to collect the income distribution data through a special large scale sample survey owing to limitations of time, it too had no alternative but to fall back upon the household consumption expenditure data so as to get a broad idea of the incidence of State indirect taxation in Uttar Pradesh. The latest data on household consumption expenditure which could be made available to the Committee related to the period July 1969 - June 1970 and the same were assumed to hold good for the fiscal year 1969-70 - the year for which the Committee analysed the distribution of tax burden. The taxes covered by the Committee in its analysis were: general sales tax, motor vehicles tax, passenger and goods tax, sales tax on motor spirit, electricity duty, entertainment and betting tax, purchase tax on sugarcane, and state excise duties. These taxes accounted for 73.61 per cent of the total taxes, amounting to Rs. 1,412.8 million, raised by the Government of Uttar Pradesh in 1969-70.

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[1]Government of Uttar Pradesh, Finance Department: Uttar Pradesh Taxation Enquiry Committee Report 1974 (lucknow, 1975), chapter III.

The next study relates to Gujarat.[1] Undertaken by the National Council of Applied Economic Research, New Delhi, at the instance of the Government of Gujarat, it estimated the tax burden by different income/expenditure groups. A specially designed sample survey was carried out to collect certain data. The survey related to the year 1967-68 and, as desired by the Government of Gujarat, was confined to the urban sector.

The taxes covered by the study were: income tax, union excise duties, sales tax (including sales tax on motor spirit), motor vehicles tax, tax on passengers carried by road, entertainment tax, electricity duty and education cess. The study did not take into account the burden resulting from taxes on non-final consumption goods like raw materials, fuel, intermediate goods, and plant and machinery.

The study of tax burden distribution in Gujarat done by the National Council of Applied Economic Research has been followed by a study done at the instance of the Gujarat Taxation Enquiry Commission which was set up by the Government of Gujarat in 1978 under the chairmanship of Raja J. Chelliah.[2] The Bureau

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[1]National Council of Applied Economic Research: Incidence of taxation in Gujarat (New Delhi, 1970), 118 pp.

[2]Government of Gujarat: Report of the Gujarat Taxation Enquiry Commission (Gandhinagar, 1980), pp. 13-20.

of Economics and Statistics, Government of Gujarat specially tabulated for the study the consumption expenditure data for the state collected during the thirty-second round (1977-78) of the National Sample Survey. To obtain a picture of the distribution of income among households in the state, the consumption estimates for the different expenditure groups derived from the NSS data were combined with the information available in a study on savings. The taxes covered by the study are: land revenue, profession tax, conversion tax, stamp duty and registration fees, general sales tax, sales tax on motor spirit, motor vehicles tax, passengers and goods tax, electricity duty, entertainment tax and state excise duties. The study has taken into account not only the burden resulting from indirect taxes falling on final consumer goods, but also that resulting from taxes on intermediate consumption goods and capital goods.

The next study relates to Karnataka (formerly Mysore). It was done by the National Council of Applied Economic Research, New Delhi.[1] Sponsored by the then Government of Mysore, the study related the tax burden to household income and expenditure and estimated the pattern of its distribution among different income and expenditure groups, both in the urban and in the rural sectors. As in the case of the Gujarat (1967-68) study, a

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[1]National Council of Applied Economic Research: Incidence of taxation in Mysore State (New Delhi, 1972), 57 pp.

specially designed sample survey was carried out to collect the necessary data.

The study relates to the year 1968-69. The taxes which were covered by the study are: income tax, central excise duties, land revenue, sales tax (including sales tax on motor spirit), state excise, motor vehicles tax, tax on passengers carried by road, entertainment tax and electricity duty.

A study has also been made to estimate the distribution of tax burden on people belonging to different economic classes in West Bengal.[1] The study relates to the year 1964-65 and is based on the household consumption expenditure data collected during the nineteenth round (July 1964 - June 1965) of the National Sample Survey. The taxes covered by the study are: central excise duty; import duty; state excise duty on alcohols and intoxicants; taxes, fees, fines, etc. on vehicles; general sales tax; sales tax on motor spirit; amusement tax; duty on consumption of electricity; and tax on entry of goods.

Another study which has been made to estimate the distribution of tax burden at the state level relates to Rajasthan.[2]

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[1] Banomali Dey: "Impact of indirect taxes on distribution of consumer expenditure", in Economic and Political Weekly, (Bombay, Sameeksha Trust), September 7, 1974, pp. 1543-1552.

[2] Shyam Nath: Incidence of important central and state taxes in Rajasthan, a thesis submitted to the University of Rajasthan for the degree of doctor of philosophy (Jaipur, 1976), 293 pp.

The study relates to 1961-62 and 1973-74 and is based on the household consumption expenditure data collected during the seventeenth round (September 1961 - July 1962) and twenty-eighth round (October 1973 - June 1974) of the National Sample Survey. The taxes covered by the study for the purpose of estimating the distribution of tax burden among different rural and urban consumption expenditure groups are: central excise duties, import duties, sales tax, state excise duties, motor vehicles tax, tax on passengers and goods, entertainment tax and electricity duty.

There have been a number of studies in addition to the ones surveyed by us.[1] The objective of many of these studies has been to obtain a quantitative basis for examining equity in taxation as between the rural and the urban or the agricultural and the non-agricultural sectors.[2] One study has analysed the

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[1]See, for example, Ved P. Gandhi: Tax Burden on Indian Agriculture (Cambridge, Massachusetts, The Law School of Harvard University, 1966), chapter 5; M.H. Gopal: Wealth Tax in India: Its Burden and Impact (New Delhi, Economic and Scientific Research Foundation, 1970), pp. 23-35; Anupam Gupta: "Income Distribution, Tax Yield and Progression in Income Taxation", Economic and Political Weekly, Vol. 7, no. 42, October 14, 1972, pp. 2111-2118; H.F. Lydall and M. Ahmed: "An Exercise in Forecasting Consumer Demand and Taxation Yields in India in 1965-66", Indian Economic Review, August 1961; Mahesh T. Pathak and Arun S. Patel, Agricultural Taxation in Gujarat (Bombay, Asia Publishing House, 1970), 93 pp; C.H. Hanumantha Rao: Taxation of Agricultural Land in Andhra Pradesh (Bombay, Asia Publishing House, 1964); G.S. Sahota: Indian Tax Structure and Economic Development (Bombay, Asia Publishing House, 1961), chapter II; and S.L. Shetty: "An Inter-Sectoral Analysis of Taxable Capacity and Tax Burden", Indian Journal of Agricultural Economics, vol. XXVI, no. 3, July-September 1971, pp. 216-246.

[2]See, for example, Ved P. Gandhi, op.cit.; and S.L.Shetty, op.cit.

available data with a view to obtaining some idea of the effective incidence of progression in the income tax rates,[1] whereas another study has analysed the aggregate burden of the income and wealth taxes at different levels of income from wealth.[2] But none of the studies attempted so far has been concerned with the estimation of distribution of tax burden resulting from all the taxes levied by the central, state and union territory governments in India. In the remainder of this section, an attempt will be made to fill this gap.

Coverage

Our study relates to the year 1975-76. It covers all the direct and indirect taxes levied by the central government and the various state and union territory governments in India. Taxes are also levied by the thousands of local authorities in the country,[3] but we make no attempt to cover them. This is largely due to the serious problems on the front of data availability.

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[1]Anupam Gupta, op. cit.

[2]M.H. Gopal, op. cit.

[3]Taxes levied by local authorities include octroi duty, terminal tax, property tax, etc.

In 1975-76, a total sum of Rs. 111,817.3 million was collected by way of all the direct and indirect taxes levied by the central, state and union territory governments in India (Table 2). Among other things, this figure includes (a) taxes paid by the central, state and union territory governments on goods purchased for consumption and capital formation, (b) taxes paid by the non-government sector on capital goods and raw materials for capital goods, and (c) taxes shifted to foreign importers of Indian goods. Taxes paid by the government sector[1] on goods purchased for consumption or capital formation do not result in a net burden on the people. These taxes should therefore be excluded from the pool of taxes allocable to the people. According to the computations made by us, these taxes amounted to Rs. 4,185.7 million in 1975-76.

As regards taxes on capital goods and raw materials for capital goods, the position is that these taxes raise the cost of capital goods and can only be passed on to the consumers of their products through higher depreciation charges. But the question is: how much on account of these taxes should be included in the pool of taxes allocable to the people in a year? If one goes through the literature, one will come up with three answers

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[1] The government sector here includes only those departments of the central, state and union territory governments whose services are given free.

TABLE 2

DETAILS OF COMBINED TAX REVENUE OF THE CENTRE, STATES AND UNION TERRITORIES 1975-76

Taxes	Amount (Rs. million)	Per cent of the total
1	2	3
1. Corporation tax (including surtax)	8,617.0	7.71
2. Taxes on income	12,143.6	10.86
3. Estate duty	116.5	0.10
4. Interest tax	583.8	0.52
5. Wealth tax	537.3	0.48
6. Gift tax	51.1	0.05
7. Stamp duties and registration fees	2,344.4	2.10
8. Land revenue	2,341.0	2.09
9. Agricultural income tax	284.8	0.25
10. Taxes on professions, calling and employment and urban immovable property tax	250.4	0.22
11. Import duties	13,361.2	11.95
12. Export duties	832.8	0.74
13. Central excise duties	38,447.8	34.38
14. State excise duties	4,574.8	4.09
15. Sales tax	20,183.4	18.05
16. Taxes on vehicles	2,087.5	1.87
17. Entertainment tax	1,399.7	1.25
18. Taxes on goods and passengers	1,858.3	1.66
19. Taxes on electricity	1,118.6	1.00
20. Foreign travel tax	82.3	0.07
21. Other taxes	601.0	0.54
Total	111,817.3	100.00

Source: Government of India, Ministry of Finance, New Delhi.

to this question. First: allocate all the taxes on capital goods in the year in which they are collected.[1] Second: allocate a sum equal to the average of last ten years' taxes levied on capital goods.[2] And third: allocate only ten per cent of the taxes on capital goods collected in a year.[3]

In our view, the second answer makes much more sense than the other two answers. Given the fact that indirect taxes on capital goods are capitalised, it is logical to expect that the market prices of consumer goods produced in a year will be influenced by indirect taxes paid on capital goods in past years. Thus, assuming the average life of capital goods to be ten years, the incidence of indirect taxes on final consumer goods can be taken as the average of last ten years' taxes levied on capital goods. Using this approach, we figure that a sum of Rs. 13,533 million - the difference between the amount of taxes on capital

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[1]See National Council of Applied Economic Research (1972), op. cit., pp. 41-42.

[2]See Banomali Dey, op. cit., pp. 1544-45.

[3]See Government of India, Ministry of Finance (Department of Revenue), op. cit., p. 113; and Government of Gujarat, op. cit., p. 17.

goods (including taxes on raw materials for capital goods) levied in 1975-76 and the average of taxes levied on such goods during the last ten years (i.e., from 1965-66 to 1974-75) - should be deducted to arrive at the effective burden of taxes on the people during the year 1975-76.

A case also exists for an adjustment on account of taxes whose incidence falls on foreign residents. Although it has been an accepted principle in India to free export of all internal commodity taxes so as to improve their competitiveness in international markets, the system which has been evolved for the grant of drawback of duties is such that the amount of drawback granted seldom equals the actual customs and excise duties paid at successive stages of the manufacture of a given export product. Further, sales taxes paid are not taken into account in the drawback calculations. The result is that the exporter gets as drawback only a part of the actual taxes paid. It is at least partly because of this inadequacy that the Government of India has had to introduce schemes of cash assistance or other forms of incentives to enable exporters to compete in overseas markets. But the costs involved in operating these schemes and incentives are not adjusted against taxes raised. All that is adjusted is the amount granted by way of drawbacks which, as stated above, does not equal the actual taxes paid. In view of this, a deduction should be made from the figure of total taxes raised, so as to arrive at the effective burden of taxes on the people

during a year. According to our computations, the deduction relevant to the year 1975-76 amounts to Rs. 2,260 million.

The three deductions which we have discussed above, add up to a total of Rs. 19,978.7 million. This means that the effective burden on the people in India as a result of the taxes levied by the central, state and union territory governments in the country, amounted to Rs. 91,838.6 million (Rs. 111,817.3 million minus Rs. 19,978.7 million) in 1975-76. Let us now proceed to analyse the distribution of this burden.

Data Used

We propose to use data from a number of sources, including the National Sample Survey Organisation of the Government of India. The twenty-eighth round of the National Sample Survey (NSS), carried out during the period October 1973 - June 1974, is a fairly comprehensive survey of household expenditure. We assume that the consumption patterns which the data collected during this round reveal, hold good for 1975-76.[1]

In the NSS data used for this study, the estimates of consumption expenditure have been given by monthly per capita expenditure classes in rupees. The expenditure levels have been

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[1]The NSS consumption expenditure data suffer from certain limitations (see Anand P. Gupta: Fiscal Policy for Employment Generation in India, An ILO-WEP Study (New Delhi, Tata McGraw-Hill Publishing Company Limited, 1977), pp. 41 and 43). While we fully recognise these limitations, we believe that the NSS data can still be used as a basis for drawing a fairly realistic picture of the distribution of tax burden in India.

grouped into 14 classes, separately for rural and urban sectors. These classes are: Rs. 0-13, Rs. 13-15, Rs. 15-18, Rs. 18-21, Rs. 21-24, Rs. 24-28, Rs. 28-34, Rs. 34-43, Rs. 43-55, Rs. 55-75, Rs. 75-100, Rs.100-150, Rs. 150-200 and Rs. 200 and above. We have regrouped these 14 classes into seven classes, namely, Rs. 0-15, Rs. 15-28, Rs. 28-43, Rs. 43-55, Rs. 55-75, Rs. 75-100, and Rs. 100 and above.

There is a difference between the figure of total consumption expenditure worked out on the basis of the NSS data and the estimate of consumption expenditure derived from national accounts (prepared by the Central Statistical Organisation, Government of India). The Central Statistical Organisation's (CSO's) figure is higher - by nearly 12 per cent. We have taken the CSO's figure for 1975-76 and have come up with estimates of consumption expenditure for each expenditure group in the rural and urban sectors on the basis of the proportions revealed by the NSS data for 1973-74.

<u>Incidence assumptions</u>

The incidence assumptions used in this study have been classified into two variants, Variant A and Variant B. This has been done to illustrate the effect of modifications in the incidence of corporation tax and export duties. Corporation tax and export duties have been selected for illustrating the effect of modifications in incidence assumptions because of the ongoing disputes concerning the incidence of these taxes. Interestingly,

it is not just the public finance experts who are involved in the disputes; the governments have also entered the field. The Government of Assam, for example, has argued that export duty on tea is a direct tax.[1] But for the Government of India, export duty is an indirect tax.

Variant A treats both corporation tax and export duties as direct taxes and therefore assumes that their incidence is not shifted. In contrast, Variant B treats both the taxes as indirect taxes and assumes that their incidence is shifted forward in the form of higher product prices. The treatment of all other taxes is the same in both Variant A and Variant B.[2]

Both the variants treat taxes on income, estate duty, wealth tax, land revenue, agricultural income tax, gift tax, taxes on professions, calling and employment and urban immovable

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[1] In a letter to the Minister of Finance, Government of India, the Assam Chief Minister has demanded Rs. 280 million to reimburse the loss in agricultural income tax due to the imposition (by the Government of India) of ad hoc export duty on tea in 1977-78. The demand is based on the reasoning that the Government of India unilaterally imposed the duty as a result of which the assessable profits of the tea companies in Assam went down by about Rs. 730 million. It has been claimed that had the export duty not been imposed, a sum of about Rs. 280 million would have accrued to the state government as agricultural income tax. For a more detailed report, see The Economic Times (New Delhi), August 16, 1978.

[2] Thus, Variant A may be regarded to represent the set of most progressive assumptions and Variant B that of least progressive assumptions.

property tax as direct taxes and therefore assume that their incidence is not shifted. Stamp duties and registration fees have also been treated as direct taxes. This can be justified on the ground that the incidence of these taxes falls mainly on property owners and is not reflected in the pricing decisions concerning consumer goods. As regards import duties, central excise duties, foreign travel tax, interest tax, state excise duties, sales tax, taxes on vehicles, taxes on goods and passengers, entertainment tax, taxes on electricity, etc., both variants treat them as indirect taxes and therefore assume that their incidence rests fully on the final consumer.

Allocation of taxes

The burden of taxes on income (other than corporation tax) has been allocated entirely to the top consumption expenditure class in the urban sector. This has been done because taxes on income, being taxes on non-agricultural income, are mostly borne by the urban population. The people who pay these taxes constitute a relatively small numerical minority and belong almost without any exception to top rungs of the economic ladder.

The burden of estate duty, wealth tax and gift tax has also been allocated entirely to the top consumption expenditure class in the urban sector. Some may object to this on the ground that the rural sector also bears the burden of these taxes. We readily concede this point, but what is important

to note is that the contribution of the rural sector to the revenue from these taxes has been very small - available evidence suggests that it did not amount to even five per cent in 1975-76. In view of this, we do not think it would make much of a difference to our results if the entire burden of estate duty, wealth tax and gift tax is allocated to the urban sector. This will turn out to be particularly so if account is taken of the fact that the total revenue from these taxes (Rs. 704.9 million) works out to only 0.77 per cent of the taxes allocated in this study.

For stamp duties and registration fees, we have followed the practice adopted by both the U.P. Taxation Enquiry Committees.[1] Thus, 80 per cent of the receipts from these duties and fees have been treated as the burden borne by the urban population and the remaining 20 per cent by the rural population. The entire burden has been allocated to the top consumption expenditure class.

Land revenue has been considered as a burden on the rural population alone. As regards its distribution among the different expenditure groups, all that we can do is to treat it as a proportional tax.[2]

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[1]See Government of Uttar Pradesh, Finance Department, op. cit., p. 88.

[2]A careful review of the literature suggests that land revenue is at best a proportional tax. See ibid., p. 107.

Agricultural income tax has also been considered as a burden on the rural population alone. It has been allocated entirely to the top consumption expenditure class.

Taxes on professions, calling and employment and urban immovable property tax have been considered as a burden on the urban population alone. The entire collections from these taxes have been allocated to the top consumption expenditure class.

We may now deal with the following taxes: import duties, central excise duties, state excise duties, sales tax, taxes on vehicles, entertainment tax, taxes on goods and passengers, tax on electricity and other taxes (e.g., newspapers and advertisement tax, education cess, taxes on raw jute). The incidence of these taxes was analysed in the study undertaken for the Jha Committee. We have relied on the results of this study for allocation of these taxes among different rural and urban consumption expenditure groups.

Let us now deal with the allocation of interest tax and foreign travel tax. Interest tax being a burden on bank borrowers, should be allocated according to the consumption pattern of the goods and services produced by them (bank borrowers). But as information along the desired lines is not available, the best we can do is to treat the tax as an excise tax and allocate its burden accordingly.

The burden of foreign travel tax has been allocated entirely to the top consumption expenditure group in the urban sector. We recognise the limitation of this approach, in that a good part of the travel subject to this tax is by people who travel on business, institutional or government expense. People belonging to rural areas (e.g., people travelling from Kerala villages to West Asian countries for employment in those countries) also bear a part of the burden of this tax. The data required for making suitable adjustments on these accounts are not available. But the point is that even if such data were available, they would not have made much difference to the results of this study. This is especially so because the collections on account of foreign travel tax amounted to a mere 0.09 per cent of the total taxes allocated in this study.

Finally, we may address ourselves to the allocation of corporation tax and export duties. In Variant A, which treats these taxes as direct taxes, their burden has been allocated entirely to the top consumption expenditure class in the urban sector. As regards Variant B, the question of allocating export duties does not arise. Since this variant treats export duties as indirect taxes, their incidence has been assumed to be shifted forward in the form of higher prices for the foreign consumer. Allocation of corporation tax, however, is a problem. Data required for allocating corporation tax, when treated as an

indirect tax, are not available. In an ideal situation, one would like to allocate its burden according to the consumption pattern of the output of the corporate sector. But as information along the ideal lines is not available, the best we can do is to treat the tax as an excise tax and allocate its burden accordingly.

Our findings

Table 3 presents the results of this study. One point emerges clearly from these results. This relates to progression of tax burden: Taxes in India are, on the whole, progressive, with the non-poor bearing a heavier tax burden than the poor do.

Before we proceed further, a word may be said about the limitations of our study. One limitation of the study is that it has measured tax burden in relation to consumption expenditure. One can argue that it would have been better if the study had measured tax burden in relation to income rather than consumption expenditure. All that we have to say is that while we readily concede this point, we were not able to relate tax burden to income as the required data on income distribution were not available.

One can say that our study suffers from another limitation in that, for estimating the incidence of taxes such as central excise duty, sales tax and taxes on goods and passengers, it has relied on the results of the tax incidence

TABLE 3

TAX BURDEN AS PER CENT OF CONSUMPTION EXPENDITURE
1975-76

Monthly per capita expenditure group (Rs.)	Rural India	Urban India	Rural and urban combined
1	2	3	4
0 - 15	3.77 (4.16)	6.37 (8.00)	3.88 (4.33)
15 - 28	4.47 (4.92)	7.27 (8.20)	4.76 (5.26)
28 - 43	5.74 (6.34)	8.43 (9.51)	6.18 (6.85)
43 - 55	7.63 (8.50)	10.99 (12.43)	8.30 (9.28)
55 - 75	8.24 (9.22)	13.32 (15.15)	9.41 (10.58)
75 - 100	11.93 (13.38)	16.40 (18.67)	13.18 (14.85)
100 and above	19.66 (22.02)	86.60 (71.40)	45.52 (41.09)
All groups	10.12 (11.30)	38.35 (34.19)	17.18 (17.02)

Note: Figures within brackets show the burden of taxes under Variant B.

study prepared for the Jha Committee. If the study had not relied on these results and had instead attempted to estimate the incidence of the taxes in question using data such as those revealed in the study by Ahmad and Stern, the resulting progression in taxes would have been of a lower order.

We believe that despite these limitations our study provides a meaningful picture of the distribution of tax burden in India.

HAS THE TAX SYSTEM DONE A GOOD JOB?

The tax system in India has done a fairly good job. One can say this because of two things. Firstly, the tax system has achieved considerable success in raising resources. It is currently raising over Rs. 310,000 million a year. This is not a small figure. Even if one compares its performance on the front of mobilisation of resources with tax systems of other countries, one will find that it is doing very well. And secondly, the tax system in India is progressive, with the non-poor bearing a heavier tax burden than the poor do.

But this does not mean that there is no scope for improvement in the performance of the tax system. Indeed, a careful examination of the relevant data clearly suggests that a lot can be done to, say, improve the progressivity of the tax system. The obvious way of achieving this is by raising more resources through direct taxes. We are convinced that if the

tax system is to be made more progressive, direct taxes will have to improve their performance. We do not believe that direct taxation in India has reached the saturation point.

Those who believe that direct taxation in India has reached the saturation point, should know that the total direct tax collections of the centre, states and union territories amount to only 3.32 per cent (1.83 per cent under Variant B) of the country's national income, and that quite a large number of people who should be paying direct taxes, do not pay them at all. A good number of those who do pay these taxes, escape by paying considerably smaller sums than what they should pay. How can one forget the results of the voluntary disclosure scheme of 1975 (under which as many as 255,782 declarations, involving concealed wealth and income of the order of Rs. 15,533.8 million, were made) and those of the special bearer bonds scheme of 1981 (under which the Government of India received as much as Rs. 9,639.27 million).

That direct taxation has not reached the saturation point will become clearer if one takes a look at what is happening on the front of estate duty. As we all know, estate duty is levied on wealth acquired without effort. It is therefore a better instrument of redistributive policy than, say, income tax because it has much less adverse effect on incentives. Estate duty becomes a still better instrument of redistributive policy if it is considered that (a) intergenerational transfer of

material wealth is a major reason for the persistence of wealth inequality, and (b) wealth inequality is more pronounced than income inequality and is recognised as a principal cause of the great disparities of economic condition in Indian society. Despite all this, estate duty continues to be an unimportant tax in India's tax system. The collections on account of estate duty have always been very small. For the year 1983-84, receipts from this tax are estimated at just Rs. 190 million. As a proportion of total tax receipts, this works out to only 0.06 per cent. In the late fifties and early sixties (1955-56 to 1965-66), the proportion was 0.23 per cent. This state of affairs is due to leakages at the level of tax policy formulation as also at the level of tax administration.

What we are trying to say is that much more money can be raised through direct taxes than what is being raised now. But for this to happen, a determined effort will have to be made to plug all the leakages in direct tax policy formulation and its administration at both the central and state and union territory levels. Experience shows that many a time these leakages have the effect of producing results which are inconsistent with the requirements of equal tax treatment of equals and unequal tax treatment of unequals. Consider, for example, the data relating to individuals in Delhi who have been assessed on an income of more than Rs. 200,000 during the financial year 1976-77.

The data show that only 35 individuals were so assessed. (Of these 35 individuals, nine are foreigners, working for organizations like the Ford Foundation.)[1] This is incredible.[2] Clearly, a large number of rich individuals have managed their affairs in such a manner that their taxable incomes do not add up to much. It also seems that many have simply resorted to under-reporting or non-reporting of their incomes. What is more, while certain high-salaried individuals have been assessed on all the income they made, many individuals making equivalent income from sources other than salary have escaped the income tax net by paying much less than what they should pay. Indeed, the income tax payable by the Delhi's super-rich works out to be less than that payable by the not-so-rich!

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[1] For details of these data, see The Economic Times (New Delhi), August 5, 1978. Data relating to more recent years are not available, but there is reason to believe that the picture has not changed much since 1976-77.

[2] It seems that it is things of this kind which are responsible, at least partly, for the outbursts of people like U.S. Congressman Long, Chairman, Sub-Committee on Foreign Operations of the House Committee on Appropriations, accusing rich Indians of evading income tax and thereby evading their responsibility for India's millions living in poverty. Mr. Long is reported to have claimed that when he was in India, he was told that "their income tax is five to ten per cent revenue and ninety per cent corruption." See The Hindustan Times (New Delhi), April 25, 1983.

If India's performance on the front of direct taxes is to be improved, at least two things will have to be done. First, a sincere effort will have to be made to improve the management of tax expenditures. And second, much more money will have to be raised from the rural non-poor than what the tax system has been able to raise so far. Sections three and four discuss these in some detail.

III. MANAGEMENT OF TAX EXPENDITURES

Tax expenditures have been defined as those provisions in a tax system that involve departures from the normative structure of the tax with the intent to encourage private behaviour in line with government objectives or to relieve hardships. Essentially, by reducing normative tax liabilities, the tax expenditures represent government monetary assistance delivered through the tax system rather than the direct budget.[1]

To illustrate, let us consider the provision relating to investment allowance. Under section 32A of the Indian Income Tax Act, 1961, a deduction on account of investment allowance is

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[1]Lotfi Maktouf and Stanley S. Surrey: "Tax Expenditure Analysis and Tax and Budgetary Reform in Less Developed Countries" (Mimeographed, 1983), p. 3.

allowed in the computation of taxable profits at the rate of 25 per cent of the actual cost of (i) new ships or new aircraft acquired by taxpayers engaged in the business of operation of ships or aircraft, (ii) new machinery and plant installed for the purposes of the business of carrying on repairs to ocean-going vessels or other powered craft, (iii) new machinery or plant installed for the purposes of business of generation or distribution of electricity or any other form of power, (iv) new machinery or plant installed for the purposes of business of construction, manufacture or production of any one or more of the articles or things specified in the Eleventh Schedule to the Income Tax Act, and (v) new machinery or plant installed in a small scale industrial undertaking for the purposes of business of manufacture or production of any articles or things. Where the plant or machinery is installed for the manufacture or production of an indigenously developed article or thing, the rate of investment allowance is 35 per cent.[1] Thus, if a company instals a new machine costing, say, Rs. 1 million for manufacturing an indigenously developed article or thing, it will be entitled to claim a deduction of Rs. 350,000 on account of investment allowance. This, using the rate of corporation tax (including surcharge) currently applicable to the generality of cases, viz., 57.75

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[1]According to a recent (1983) amendment, investment allowance at the higher (35 per cent) rate is also available in respect of machinery or plant which would assist in pollution control or protection of environment.

per cent (55 per cent + 5 per cent thereof), will enable the company to reduce its tax liability by Rs. 202,125. In other words, investment allowance provides government assistance to the company.[1] But since the allowance provides government assistance through reduction in tax liability rather than direct aid, it qualifies for treatment as a tax expenditure.

The provision relating to investment allowance is not the only one which qualifies for treatment as tax expenditure. One can readily identify many other provisions in the Income Tax Act which are "special" and represent tax expenditures. Examples are: house rent allowance (sections 10(13A) and 80GG); exemption in respect of income from interest on capital investment bonds (section 10(15)(iib); exemption of income from newly established industrial undertakings in free trade zones (section 10A); additional depreciation allowance (section 32(1)(iia); deduction in respect of capital expenditure on scientific research (section 35(2)(ia); weighteddeduction in respect of donation for scientific research undertaken under an approved programme (section 35(2A); weighted deduction in respect of any expenditure incurred by an assessee on scientific research undertaken under an approved programme (section 35(2B)(a); agricultural development allowance

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[1]Investment allowance is in addition to the normal depreciation allowances and is not taken into account for determining the written down value of the plant and machinery to which it applies. Hence the allowance acts as a bonus or special allowance over and above the normal recoupment of the cost of plant and machinery through depreciation allowances.

(section 35C); rural development allowance (section 35CC); deduction in respect of payment to associations and institutions for carrying out programmes of conservation of natural resources (section 35CCB); deduction in respect of life insurance premia, contributions to provident fund, etc. (section 80C); deduction in respect of investment in equity shares of new industrial companies and public housing finance companies (section 80CC); deduction in respect of medical treatment of handicapped dependants (section 80D); deduction in respect of donations for charitable purposes (section 80G); deduction in respect of any sum paid by a taxpayer to the National Fund for Rural Development (section 80GGA); deduction in respect of profits and gains from newly established industrial undertaking or hotel business in backward areas (section 80HH); deduction in respect of profits and gains from newly established small scale industrial undertakings in certain areas (section 80HHA); deduction in respect of profits and gains from projects outside India (section 80HHB); tax concession based on export turnover (section 80HHC); deduction (tax holiday) in respect of profits and gains from new industrial undertakings, etc. (sections 80I[1] and 80J); deduction in respect of profits and gains from business of livestock breeding, poultry and dairy farming (section 80JJ);

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[1]Section 80I, as it stands now, deals with tax holiday benefit to new industrial undertakings, etc. Earlier, it dealt with special tax benefit available in respect of profits of companies from priority industries.

deduction in respect of interest on certain securities, dividends, etc. (section 80L); deduction in respect of inter-corporate dividends (section 80M); deduction in respect of dividends received from certain foreign companies (section 80N); deduction in respect of royalty, commission, fees, etc. from foreign enterprises (section 80-O); deduction in respect of remuneration from certain foreign sources in the case of professors, teachers and research workers (section 80R); deduction in respect of professional income from foreign sources in certain cases (section 80RR); deduction in respect of remuneration received for services rendered outside India (section 80RRA); deduction in the case of totally blind or physically handicapped resident persons (section 80U); and special provisions relating to taxation of income from certain specified assets in the case of non-resident Indian citizens and foreign nationals of Indian origin (section 115C).

It is not just the Income Tax Act which includes provisions that result in tax expenditures. Other direct tax laws also include such provisions. Indeed, if one takes a careful look at the provisions in the various direct tax laws, one would find that the Indian tax system is honeycombed with tax expenditures.

Tax expenditures have become so popular that practically all government committees set up to look into specific problems of public policy have come up with recommendations for introduction, extension, enlargement or maintenance of tax expenditures.

Thus, the Task Force on Marine Products Industry, set up by the Government of India in April 1981, is reported to have recommended the grant of tax holiday benefits to fishing vessels. The Task Force has also recommended raising of investment allowance entitlement from 25 per cent to 40 per cent. These special incentives, the Task Force believes, will promote deep-sea fishing.[1] The Committee on Free Trade Zones, which submitted its final report to the Government of India recently, feels that tax holiday of five years offered to free trade zone enterprises in the 1981-82 budget is inadequate. This, according to the Committee, should be extended to ten years and even after that further concession should be granted on a case by case basis.[2] The Planning Commission's Study Group on Financing of the Private Corporate Sector has recommended that a deduction by way of advance investment allowance should be permitted in the computation of taxable profits for amounts deposited with the Industrial Development Bank of India to assist companies to accumulate funds for undertaking new investment at the appropriate time and in a phased manner. The Group is of the view that investment/in equities should also be encouraged. It has, therefore, recommended that the deduction

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[1]For a press report on the recommendations of the Task Force, see <u>The Hindustan Times</u> (New Delhi), September 15, 1982.

[2]For a press report on the report of the Committee, see <u>The Hindustan Times</u> (New Delhi), September 25, 1982, pp. 1 and 8.

available under section 80L of the Income Tax Act should be thrown open to dividend income on the same footing as interest on bank deposits and income from units issued by the Unit Trust of India. In addition, the Group has recommended that a deduction of 15 per cent should be allowed from dividend income in excess of the amount exempted under section 80L. Certain other recommendations to encourage investment in equities have also been made, such as lowering of the rate of deduction of tax at source from dividend on equities.[1]

When people look for financial support for any public cause, they generally end up with pleas for government support through the tax system. Let me give one recent example. There is an organisation called Dardionu Rahat Fund which provides medicines, fruits, and other requirements to poor patients free of cost. The Fund recently organised a function which was attended, among others, by Mr. Pranab Mukherjee, Finance Minister, Government of India, and Mr. P N Bhagwati, Justice, Supreme Court of India. Speaking at the function, Mr. Justice Bhagwati is reported to have urged the Finance Minister to help the Fund in securing recognition for it so that the donations received by it are exempted from tax.[2] One wonders why Mr. Justice Bhagwati

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[1]For a press report on the recommendations of the Study Group, see The Hindustan Times (New Delhi), May 21, 1983, pp. 1 and 7.

[2]See The Times of India (Ahmedabad), September 26, 1982, p. 3.

urged the Finance Minister to provide governmental financial support through the tax system rather than through direct government aid.

Then, there are organisations like the Federation of Indian Chambers of Commerce and Industry, the Associated Chambers of Commerce and Industry, the Punjab, Haryana and Delhi Chamber of Commerce and Industry, the Indian Merchants' Chamber, the Gujarat Chamber of Commerce and Industry, and the Indian Chamber of Commerce which are always ready with proposals for introduction, extension, enlargement, or maintenance of tax expenditures and keep on lobbying for them. The Federation of Indian Chambers of Commerce and Industry, for example, is lobbying these days for (a) raising investment allowance entitlement from 25 per cent to 45 per cent for those industrial enterprises that go in for modernisation; (b) introduction of a provision allowing a deduction in respect of profits set apart for replacement of plant and machinery and modernisation; (c) broadening the scope of section 80-O of the Income Tax Act so that the entire royalty, commission, fee, and similar incomes qualify for 100 per cent deduction under this section and no part thereof is subjected to tax on the ground that it relates to the rendering of management and other such incidental services; (d) extension of section 80-O benefit to non-corporate taxpayers; (e) extension of section 80-O benefit to all the partners of a consortium when a consortium is formed to provide technical know-how to foreign enterprises; (f) broadening the scope of section 80N so that one can claim

deduction in respect of dividend income from investments in joint ventures abroad irrespective of mode of investment; (g) extension of section 80N benefit to non-corporate taxpayers; (h) raising deduction under section 80RRA from the present level of 50 per cent to 100 per cent; (i) raising deduction under section 80HHB from the present level of 25 per cent to a higher level; and so on.[1]

The Government of India as also the different state and union territory governments in the country seem to have a soft corner for tax expenditures. They generally respond favourably to demands for introduction, extension, enlargement and maintenance of tax expenditures. But what about the accounting of these expenditures? Do we know how many tax expenditure provisions the various direct tax laws in India contain and how much governmental financial assistance is provided through these provisions?

The Directorate of Inspection (Research, Statistics and Public Relations) in the Department of Revenue, Ministry of Finance, Government of India brings out a publication titled

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[1]See The Economic Times (Bombay), September 8, 1982, p. 4; Federation of Indian Chambers of Commerce and Industry, Workshop on Indian Joint Ventures Abroad and Project Exports-Report (New Delhi, 1982), pp. 22-28; and 16th All India Conference of Corporate Managers and Tax Executives (22-23 October, 1982): Background Paper (New Delhi, 1982), pp. 2-9.

All India Income Tax Statistics (AIITS) which provides, among other things, data on deductions allowed and tax relief granted under a number of provisions in the Income Tax Act. Table 4 presents these data in respect of assessments completed during the years 1968-69, 1969-70, 1971-72, 1972-73, 1974-75, 1975-76, 1976-77, 1977-78, 1978-79 and 1979-80.[1] The data for 1970-71[2] and 1973-74[3] are not available.

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[1]1979-80 is the latest year for which All India Income Tax Statistics is presently available.

[2]According to a statement in All India Income Tax Statistics for 1971-72, the compilation of all India income tax statistics for 1970-71 "has been kept in abeyance."

[3]It appears that the compilation of all India income tax statistics for 1973-74 has also been kept in abeyance.

TABLE 4

DEDUCTIONS ALLOWED IN INCOME TAX ASSESSMENTS COMPLETED DURING THE YEARS 1968-69 TO 1979-80

Assessment Year	Contributions to provident fund, life insurance, etc. (Sec. 80 C)	Expenditure on medical treatment etc. of handicapped dependents (Sec. 80 D)	Payments for securing retiring benefits (Sec. 80 E)	Educational expenses abroad of children of non-citizens (Sec. 80 F)	Donations for charitable purposes (Sec. 80 G)	Profits of undertakings employing displaced persons (Sec. 80 H)	Profits of companies from priority industries (Sec. 80 I)
1	2	3	4	5	6	7	8
1968-69							
A	696,617	7,768	4,891	139	3,210	177	2,540
B	80,356	973	1,252	44	1,524	75	1,457
C	892,231	8,140	3,568	186	1,402	106	72
1969-70							
A	770,775	3,350	1,079	506	11,086	1,403	21,047
B	98,362	432	233	164	5,466	684	11,897
C	965,555	3,210	815	708	3,624	412	163
1971-72							
A	957,331	1,429	691	579	24,642	11,594	93,484
B	139,355	240	170	168	13,249	6,248	50,057
C	1,045,667	1,220	537	435	4,428	465	395
1972-73							
A	1,150,326	789	354	213	23,591	2,752	66,584
B	142,697	101	121	69	12,524	1,845	37,703
C	1,112,871	684	184	174	4,198	232	295

Assessment Year	Profits from new industrial undertakings, etc. (Sec. 80 J)	Dividends from new industrial undertakings etc. (Sec. 80 K)	Dividends from Indian companies, interest from securities, bank deposits etc. (Sec. 80 L)	Inter-corporate dividends (Sec. 80 M)	Royalty etc. from companies (Sec. 80 MM and 80-O)	Dividends from foreign companies (Sec. 80 N)	Income of cooperative societies (Sec. 80 P)
	9	10	11	12	13	14	15
1968-69							
A	2,006	5,870	1,635	29,246	9,319	194	7,431
B	1,119	3,395	632	19,738	8,180	84	1,860
C	122	1,201	2,746	157	4	5	244
1969-70							
A	19,645	18,305	32,895	84,647	548	889	8,729
B	9,953	10,118	18,629	55,930	338	622	2,451
C	1,584	3,460	15,905	381	5	5	673
1971-72							
A	65,876	55,675	112,394	214,464	1,515	3,294	21,986
B	36,033	31,909	49,730	124,848	975	2,081	6,860
C	1,080	4,387	42,145	669	10	24	1,435
1972-73							
A	164,675	31,480	71,925	239,571	2,428	2,102	40,241
B	91,115	18,081	17,986	158,338	1,686	1,346	11,706
C	634	3,143	41,248	806	12	17	929

	Dividends from co-operative societies (Sec. 80 Q)	Foreign remuneration of professors, teachers, etc. (Sec. 80 R)	Compensation for termination of managing agency, etc (Sec. 80 S)	Long term capital gains (Sec. 80 T)	Allowance for blind or physically handicapped persons (Sec. 80 U)	Annuity Deposits (Sec. 280-O)	Other deductions	Total
	16	17	18	19	20	21	22	23
1968-69								
A	476	80	26	4,095	191	407,958	8,686	1,192,555
B	95	34	6	1,233	33	154,079	4,472	280,641
C	194	37	18	587	113	138,188	1,770	
1969-70								
A	510	352	254	9,268	456	312,294	20,489	1,318,527
B	98	73	70	3,517	106	116,884	7,712	343,739
C	768	325	193	1,209	311	98,759		
1971-72								
A	15,111	773	1,051	34,806	2,606	89,149	139,230	1,847,680
B	8,006	156	266	15,564	981	33,248	63,638	583,782
C	685	481	198	1,963	559	28,569	27,371	
1972-73								
A	2,928	509	273	21,318	1,174	14,636	95,017	1,932,886
B	995	106	67	10,499	321	4,491	44,330	556,127
C	369	258	67	1,232	236	5,231	20,192	

1	2	3	4	5	6	7	8	9	10	11	12	13
1974-75												
A	1,691,502	516	238	237	20,810	728	18,085	48,642	32,198	121,917	143,953	2,049
B	190,557	70	112	98	10,714	243	10,134	27,084	19,274	35,057	97,754	1,153
C	1,267,010	407	84	168	4,247	345	95	704	3,647	60,654	699	9
1975-76												
A	2,066,176	760	215	405	24,467	1,180	11,569	34,593	23,728	98,815	121,802	384
B	217,732	92	69	83	12,700	432	6,480	19,923	13,504	22,660	80,030	226
C	1,150,630	605	98	149	4,276	267	29	550	3,401	58,694	633	9
1976-77												
A	2,906,409	528	492	376	22,756	909	31,848	36,799	24,949	101,328	166,905	83
B	345,624	103	99	137	10,739	184	18,330	20,871	14,108	21,723	108,833	48
C	1,159,563	339	183	162	4,438	278	13	427	2,844	55,374	691	2
1977-78												
A	3,242,915	1,092	228	272	21,225	2,141	10,974	43,893	24,071	99,357	123,481	538
B	349,740	130	62	54	10,846	1,147	6,127	24,745	12,484	19,069	74,763	368
C	1,204,844	515	70	156	4,066	164	22	408	2,591	56,355	760	3
1978-79												
A	2,333,737	1,038	138	116	24,753	2,599	3,780	65,071	36,369	78,048	72,194	4,231
B	317,124	162	28	30	13,413	1,180	2,187	37,043	19,167	16,707	46,727	2,772
C	801,436	532	59	82	3,223	156	11	458	1,900	38,455	498	12
1979-80												
A	2,341,299	322	48	87	27,378	3,865	18,919	258,452	37,950	53,337	84,977	6,848
B	336,651	43	24	30	13,973	2,074	10,743	134,489	22,455	11,613	50,815	3,968
C	823,892	184	14	30	2,160	95	10	234	1,210	24,660	583	9

	14	15	16	17	18	19	20	21	22	23
1974-75										
A	2,850	28,301	1,239	246	702	37,926	895	8,354	168,782	2,330,170
B	2,085	8,416	370	74	175	18,614	221	2,732	73,598	498,535
C	12	909	163	83	99	2,699	166	2,837	32,691	
1975-76										
A	553	65,384	2,429	266	345	49,153	1,656	6,369	119,907	2,630,176
B	351	14,413	376	78	83	24,821	310	1,925	57,471	473,759
C	12	1,232	305	97	65	2,908	308	1,961	13,214	
1976-77										
A	988	106,968	4,149	572	466	48,401	1,135	3,856	93,133	3,553,050
B	599	37,601	1,085	153	165	25,007	289	1,373	38,839	695,910
C	4	1,202	237	140	85	2,759	274	1,008	11,090	
1977-78										
A	139	100,964	3,415	369	400	35,788	719	2,673	218,683	3,933,337
B	84	31,918	942	102	53	17,980	143	819	111,321	662,897
C	5	1,093	178	46	75	1,897	176	1,023	9,676	
1978-79										
A	568	72,036	1,637	342	700	30,433	608	1,976	119,169	2,849,593
B	322	21,933	534	93	398	12,071	162	621	47,959	540,633
C	15	875	188	53	58	1,471	157	937	10,937	
1979-80										
A	2,295	32,406	444	296	66	17,758	547	1,515	132,191	3,021,000
B	1,330	9,946	195	56	12	8,400	131	264	70,897	678,109
C	7	635	37	30	24	848	130	614	5,257	

A: Amount of deductions allowed (in thousands of rupees)
B: Tax relief (in thousands of rupees)
C: Number of assessments in which the deduction in question was allowed.

Source: See text.

According to these data, the income tax relief allowed on account of various deductions ranged between Rs. 280.64 million in 1968-69 and Rs. 695.91 million in 1976-77, and amounted to Rs. 678.19 million in 1979-80. As a percentage of revenue from income tax, it ranged between 2.23 per cent in 1978-79 and 5.79 per cent in 1971-72, and stood at 2.48 per cent in 1979-80. In other words, according to the AIITS data, the tax relief which the Government of India provides through various income tax deductions does not amount to much.

This is incredible. A careful examination reveals that the AIITS data suffer from two major limitations. Firstly, these data do not cover all special deductions available under the various provisions of the Income Tax Act. Take, for example, the deductions on account of development rebate and investment allowance. The development rebate, which was in operation from April 1, 1955 to May 31, 1974,[1] has been of considerable assistance to Indian industry. An exercise undertaken in 1971 by the Ministry of Finance showed that development rebate resulted in a tax relief to industry of Rs. 700 million in 1970-71 and that the figure might go up to Rs. 850 million in 1973-74.[2] Unfortunately, the AIITS

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[1]In certain cases the development rebate was allowed if plant and machinery was installed before June 1, 1975. For ships, the rebate was available up to the end of 1976.

[2]See the reply of the Finance Minister, Government of India, to the debate in the Rajya Sabha on the Finance (No.2) Bill, 1971.

data do not cover deductions allowed on account of development rebate.

The provision relating to investment allowance was introduced in 1976. As things stand, investment allowance is a major tax concession in India. According to an estimate made by an expert committee of economists and tax administrators appointed by the Government of India, the total deduction on account of investment allowance amounted to Rs. 3,000 million in 1979-80, involving a tax relief of about Rs. 1,750 million.[1] Unfortunately, the AIITS data on deductions do not cover even investment allowance.

Secondly, even the data on deductions which the AIITS covers, do not appear to be complete. Take, for instance, the AIITS data on deductions allowed under sections 80J (tax holiday), 80MM, and 80-O (royalties etc. from companies) of the Income Tax Act. According to these data, section 80J deductions amounting to Rs. 34.59 million and Rs. 36.80 million, involving tax reliefs of Rs. 19.92 million and Rs. 20.87 million, were allowed in assessments completed during 1975-76 and 1976-77, respectively. These figures are not complete. The whole issue was studied in detail by the Expert Committee on Tax Measures to Promote Employment.

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[1]Government of India, Ministry of Finance, Department of Revenue, <u>Report of the Expert Committee on Tax Measures to Promote Employment</u> (New Delhi, 1980), p. 31.

According to the data which the Committee was able to get from the Income Tax Department, the deductions allowed to the corporate assessees under section 80J amounted to Rs. 323 million and Rs. 336.4 million in 1975-76 and 1976-77, respectively. This resulted in a tax relief of Rs. 155.2 million in 1975-76 and Rs. 183 million in 1976-77. Allowing for the fact that these figures relate to corporate assessees only, the total tax relief allowed under section 80J has been put by the Committee at Rs. 200 million in 1976-77.[1] Thus, if one compares the AIITS figure for tax relief through section 80J with that reported by the Expert Committee on Tax Measures to Promote Employment, one finds the latter to be 9.58 times the former. This is not a happy state of affairs, especially in view of the fact that the source of data in both cases is the same, viz. the Income Tax Department.

As regards data on deductions allowed under sections 80MM and 80-O, the state of affairs does not appear to be any better. Sections 80MM and 80-O have been on the statute book since April 1, 1970 and April 1, 1968 respectively. According to the AIITS, the total number of assessments in which deductions under these sections were allowed during 1968-69, 1969-70, 1971-72, 1972-73, 1974-75, 1975-76, 1976-77, 1977-78, 1978-79, and 1979-80 is 75. But according to the information furnished by the Finance Secretary, Government of India, during the course of a recent (1981) evidence

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[1] Ibid, pp. 31-32.

before the Public Accounts Committee, the number of cases dealt with under section 80-O alone is 1,103.[1] Similar information in respect of section 80MM is not available. But considering the fact that a special cell known as 80MM cell has been created for scrutinising the agreements received in the Central Board of Direct Taxes for approval under section 80MM, the number of cases dealt with under this section may be quite high. All this suggests that the 80MM and 80-O assessments - and consequently the deductions allowed and the tax relief provided under these sections - have been substantially higher than the figures indicated in the AIITS.

One thing emerges clearly from the foregoing discussion: There is no proper system of accounting of tax expenditure assistance provided through the route of income tax in India. The Directorate of Inspection does bring out some data on special deductions available under the Income Tax Act, but they lack credibility. One wonders why the Directorate keeps on bringing out these data. Is it that the Directorate is not aware of the serious limitations these data suffer from? Or is it that the Directorate, though aware of the limitations, has some other purpose in mind? One does not know what it could be. But one thing is certain: The data which the Directorate brings out are used by some as evidence to show that the tax relief which the Government of India provides through the

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[1]Lok Sabha Secretariat, Fifty-first Report, Public Accounts Committee (1980-81) (New Delhi, 1981), p. 16.

various income tax deductions does not amount to much. Take, for example, the Federation of Indian Chambers of Commerce and Industry. According to the Federation, the incentive provisions in the Indian income tax law "do not give significant relief."[1]

It is not correct to say that the incentive provisions in the Indian income tax law do not give significant relief. As things stand, the various incentive provisions in the Indian income tax law are such that they enable a large number of taxpayers to generate substantial tax savings.[2] It is because of the various incentive provisions that many companies in India pay little or no income tax (see Table 5).

One may now ask: What about the accounting of a tax expenditure assistance provided through the routes of other direct taxes such as wealth tax, gift tax, and estate duty? The answer to this question is quite simple: There exists no system of accounting of tax expenditure assistance provided through such taxes.

Considering the extensive use which policymakers in India make of the instrument of tax expenditures, what is needed is proper management of all tax expenditures. Four points are involved here.

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[1]See Federation of Indian Chambers of Commerce and Industry, op. cit., p. 3.

[2]For a discussion on how the various incentive provisions in the Indian income tax law enable companies to generate substantial tax savings, see Anand P. Gupta, "Management of the Income Tax Function: Is India a Tax Haven?", Economic and Political Weekly, Vol. XVI, No. 9, February 28, 1981, pp. M 15-21.

TABLE 5

TAXATION OF CORPORATE INCOME IN INDIA: 20 EXAMPLES

	Corporation	Period	Profit before tax (Rs. million)	Profit after tax (Rs. million)	Tax Liability (Rs. million)
1.	Tata Engineering and Locomotive	1979-80	176.2	176.2	0
		1980-81	243.7	243.7	0
		1981-82	418.8	418.8	0
2.	Reliance Textile Industries	1980	112.1	112.1	0
		1981	197.0	197.0	0
		1982	291.6	291.6	0
3.	Modi Rubber	1979-80	55.9	55.9	0
		1980-81	68.6	68.6	0
		1981-82	80.5	80.5	0
4.	Bombay Dyeing and Manufacturing	1979-80	53.4	53.4	0
		1980-81	50.2	50.2	0
		1981-82	30.4	30.4	0
5.	J.K. Synthetics	1979	97.4	97.4	0
		1980	67.0	67.0	0
		1981	120.0	120.0	0
6.	Ashok Leyland	1980	126.5	126.5	0
		1981	150.5	150.5	0
		1982	107.3	107.3	0
7.	Ahmedabad Electricity	1979-80	21.3	21.3	0
		1980-81	58.6	58.6	0
		1981-82	69.7	69.7	0
8.	Andhra Cement	1979-80	4.4	4.4	0
		1980-81	6.2	6.2	0
		1981-82	15.5	15.5	0

9. Gabriel India	1979-80	3.4	3.4	0
	1980-81	5.0	5.0	0
	1981-82	5.8	5.8	0
10. K S B Pumps	1979	3.7	3.7	0
	1980	4.9	4.9	0
	1981	15.5	11.0	4.5
11. Kunal Engineering	1979-80	5.3	5.3	0
	1980-81	6.5	6.5	0
	1981-82	12.4	12.4	0
12. Mahindra Ugine Steel	1979	31.5	31.5	0
	1980	35.2	35.2	0
	1981	71.0	71.0	0
13. Milkfood	1979	2.5	2.5	0
	1980	3.0	3.0	0
	1981	6.4	6.4	0
14. Modipon	1979	28.3	25.1	3.2
	1980	21.3	21.3	0
	1981	30.1	30.1	0
15. Nagarjuna Steels	1978-79	4.8	4.8	0
	1979-80	5.4	5.4	0
	1980-81	10.2	10.2	0
16. Punjab Anand Batteries	1979-80	4.1	4.1	0
	1980-81	5.0	5.0	0
	1981-82	4.0	4.0	0
17. Raunaq International	1979-80	1.1	1.1	0
	1980-81	1.1	1.1	0
	1981-82	1.6	1.6	0
18. Shree Vallabh Glass	1979-80	11.3	9.7	1.6
	1980-81	36.7	36.7	0
	1981-82	39.5	39.5	0

19. Steel Tubes of India	1979-80	2.4	2.4	0
	1980-81	3.8	3.8	0
	1981-82	3.1	3.1	0
20. Usha Martin Black	1979	10.7	10.7	0
	1980	16.3	16.3	0
	1981	17.3	17.3	0

Source: Compiled by the author.

The first is concerned with identifying tax expenditures. In order to identify tax expenditures, one will have to take a careful look at the various provisions in a tax law. Not all provisions allowing exemptions, deductions, etc. constitute tax expenditures. It is only special provisions in a tax law which constitute tax expenditures. These special provisions really have nothing to do with the essentials of a tax, nothing to do with shaping the structural framework necessary to operate a tax. Instead, they are methods of spending government funds.[1] Take, for example, the provision allowing a deduction of 20 per cent in respect of profits and gains from newly established industrial undertakings or hotel business in backward areas (section 80HH of the Income Tax Act, 1961). This provision is not essential for operating an income tax. It is a special provision: Its purpose is simply to provide governmental assistance. It is, therefore, a tax expenditure.

The second point is concerned with measurement of tax expenditures. One way of measuring tax expenditures is to figure out the decrease in tax receipts caused by a tax expenditure provision. The other way of measuring tax expenditures is to figure out the amount of spending that would be required to provide an equal after-tax benefit to the taxpayer. This method makes the tax expenditure data more comparable with direct budget outlays.

The third point is concerned with inclusion of the estimates of tax expenditures in the budget. Tax expenditures

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[1]Stanley S. Surrey: Pathways to Tax Reform: The Concept of Tax Expenditures (Cambridge, Massachusetts, Harvard University Press, 1973), p. 32.

are similar in purpose to direct government expenditures. What this implies is that if a government which provides assistance through tax expenditures and presents a budget which does not include estimates of tax expenditures, one will be justified in treating such budget as an incomplete budget. The budget of the Government of India belongs to this category: The Government of India provides enormous assistance through tax expenditures, and yet its budget does not include any estimate of these expenditures.

In my view, if a government provides assistance through tax expenditures, its budget must include estimates of these expenditures. It will be useful if tax expenditure estimates are grouped together by functional categories used for direct government expenditures. When including tax expenditures in a budget, one will have to take into account projected economic factors and any changes in tax expenditures resulting from proposals contained in the budget.

The inclusion of estimates of tax expenditures by functional categories in the budget will enable one to find out total government expenditure under each of the functional areas.[1] It will also enable one to figure out how tax expenditures compare with

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[1]Certain tax expenditures interact with other tax expenditures and thus affect their value. This being so, tax expenditure estimates cannot simply be added together to obtain totals for functional areas or a grand total. One will, therefore, have to make some adjustment for the interaction effects in order to obtain accurate totals.

direct government expenditures in different functional areas. For some budget functions, tax expenditures may be quite high relative to direct expenditures. Further, inclusion of estimates of tax expenditures in the budget may encourage government to consider them in budget decisions.

The fourth point is concerned with controlling tax expenditures. There appears to be a strong case for controlling tax expenditures.[1] A careful look at available evidence shows that many of the tax expenditure provisions are such that they damage the equity of the tax system, make the tax system more complex, enlarge tax avoidance possibilities, or add to costs of tax administration. Take, for example, sections 80MM and 80CC of the Income Tax Act. Section 80MM, which was put into the Income Tax Act through the Finance Act, 1969, provides for a deduction of 40 per cent of the income received by an Indian company by way of royalty, commission, fee, or any other payment (not being income chargeable under the head "capital gains") from any person carrying on a business in India in consideration for (i) the provision of technical know-how which is likely to assist in the manufacture or processing of goods or materials, or in the installation or erection of machinery or plant for such manufacture or processing, or in the working of a

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[1]See Amaresh Bagchi, "Efficacy of Tax Incentives: 'Tax Expenditure Analysis' and Its Relevance for India", Economic and Political Weekly, Vol. IX, No. 24, June 15, 1974, pp. 951-60.

mine, oil well or other source of mineral deposits, or in the search for, or discovery or testing of, mineral deposits or the winning of access to them, or in carrying out any operation relating to agriculture, animal husbandry, dairy or poultry farming, forestry or fishing, or (ii) rendering services in connection with the provision of such technical know-how. The aim underlying this section is to minimise repetitive import of technical knowhow and encourage Indian companies to develop their technical knowhow.[1]

The benefit under section 80MM is subject to the approval of an agreement for the purpose by the Central Board of Direct Taxes, Ministry of Finance, Government of India. The Board has issued detailed guidelines (circular no. 140 dated July 6, 1974) for approval of agreements under the section. A special cell has been created for scrutinising agreements received in the Board for approval under the section. For the facility of scrutiny of agreements, an applicant is required to furnish certain information in a proforma prescribed for the purpose. The head of the special cell scrutinises each of the agreements in the light of the information received and, if necessary, he may call for further information or grant a hearing to the applicant. He then puts up a note containing his recommendation as to the extent to which the agreement qualifies for approval. The Board Member In-charge

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[1]See Government of India, Explanatory Memorandum on the Finance Bill, 1969 (New Delhi), paragraphs 55-56.

takes a decision in the light of the note submitted by the head of the special cell and material on record. If necessary, he also grants a hearing to the applicant.

If the agreement is approved, the Board informs the concerned Income Tax Officer (ITO). The ITO, before allowing the benefit under the section to the party, has to familiarise himself with the section. He must also study the circular issued by the Board on the subject.

In case the Board refuses approval to the agreement, the applicant may take the matter to a court of law. Indeed, there are cases of companies which have moved the courts in writ petitions challenging the legality of the Board's refusal to approve agreements under section 80MM. All this certainly damages simplicity of the tax system and adds to costs of tax administration.

There is at least one more thing which section 80MM has done: It has enlarged tax avoidance possibilities. The scope of the section is so wide that even with the best of efforts the benefit under it cannot be limited only to those for whom it was intended. Detailed information on the working of the section is not available, but a look at whatever information is available clearly suggests that the section has also been used by those for whom it was not intended. Take, for example, the case of Lurgi India Private Limited. The company was incorporated for the purpose of obtaining consultation and technical knowhow from

Lurgi Gesellschaften, Frankfurt. It entered into two agreements with Godrej Soaps Private Limited, an Indian company, for provision of technical knowhow and technical services. The agreements, both dated May 22, 1972, were sent to the Central Board of Direct Taxes for approval under section 80MM. The Board refused approval on the ground that the technical knowhow passed on by Lurgi India to Godrej Soaps as also technical services rendered by Lurgi India to Godrej Soaps were, in fact, done by Lurgi Gesellschaften, a foreign company, through Lurgi India, an Indian company. Lurgi India filed a writ petition against the Board's orders before the Delhi High Court. The Court has held that there is no bar in section 80MM for an Indian company, which claims the benefit under this section, to obtain technical knowhow and processes from a foreign company. The Court has quashed the Board's order and directed the Board to reconsider the application of Lurgi India for grant of approval.[1]

Let us now move on to section 80CC. This section was put into the Income Tax Act through the Finance Act, 1978. Under this section, individuals, Hindu undivided families, or associations of persons investing in equity shares forming part of any eligible issue of capital are entitled to a deduction in the computation of taxable income of 50 per cent of the amount invested in such shares. The aggregate investment in a year qualifying for this deduction is limited to Rs. 20,000. For the purpose of this section, "eligible

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[1]The Judgment of the Court is reported in The Income Tax Reports, Vol. 121 (1980), pp. 141-42.

issue of capital" means an issue of equity shares which satisfies the following conditions: (a) the issue is made by a public company formed and registered in India with the main object of carrying on the business of (i) construction, manufacture, or production of any article or thing, not being an article or thing specified in the list in the Eleventh Schedule, or (ii) providing long-term finance for construction or purchase of houses in India for residential purposes; (b) the issue is an issue of capital made by the company for the first time; and (c) the shares forming part of the issue are offered for subscription to the public.

Two points may be noted here. The first relates to the impact of section 80CC on the equity of the income tax system. The section provides for a deduction of 50 per cent of the amount invested in eligible equity shares. This means that if an individual belonging to the taxable income bracket of over Rs. 100,000 buys eligible equity shares of Rs. 2,000, the effective cost to him will be as low as Rs. 1,325 - Rs. 2,000 minus tax benefit of Rs. 675.[1] If an individual belonging to the taxable income bracket of Rs. 15,000 - 20,000 also buys eligible equity shares of Rs. 2,000, the effective cost to him will be Rs. 1,719 - Rs. 2,000 minus tax benefit of Rs. 281.[2]

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[1]The figure of Rs. 675 has been arrived at by applying the marginal rate of income tax (including surcharge) currently applicable to taxable income in excess of Rs. 100,000.

[2]The figure of Rs. 281 has been arrived at by applying the marginal rate of income tax (including surcharge) currently applicable to taxable income exceeding Rs. 15,000 but not exceeding Rs. 20,000.

In other words, while both individuals invest equal amounts, tax benefit to the rich individual works out 140.21 per cent higher than that to the less well-off individual. What is worse, there is no provision for any benefit if equity shares are bought by, say, an industrial worker who does not belong to the income tax-paying fraternity.

The damage which section 80CC does to the equity of the tax system is thus obvious. There are some other sections (e.g. sections 80C and 80L) which are equally damaging.

The second point relates to the Eleventh Schedule to the Income Tax Act. As indicated above, one can claim benefit under section 80CC if one invests in equity shares issued by a public company which is engaged in the business of construction, manufacture, or production of any article or thing, not being an article or thing specified in the Eleventh Schedule. When the section was introduced, the Schedule contained 29 groups of articles or things. The Schedule was reviewed in 1981. As a result of this review, the following 14 groups were removed from the Schedule: broadcast television sets, radios (including transistor sets), radiograms and tape recorders (including casette recorders and tape decks); electric fans; domestic electrical appliances; household furniture, utensils, crockery and cutlery; pressure cookers; vacuum flasks and other vacuum vessels; tableware and sanitaryware; glass and glassware; chinaware and porcelainware; mosaic tiles and glazed tiles; organic surface active agents, surface active preparations and

washing preparations whether or not containing soap; synthetic detergents; pigments, colours, paints, enamels, varnishes, blacks and cellulose lacquers; and amplifiers or any other apparatus used for addressing the public. With the removal of these groups, the Eleventh Schedule now contains 15 groups. These are: beer, wine and other alcoholic spirits; tobacco and tobacco preparations such as cigars and cheroots, cigarettes, chewing tobacco and snuff, biris, smoking mixtures for pipes and cigarettes; cosmetic and toilet preparations; tooth paste, dental cream, tooth powder and soap; aerated waters in the manufacture of which blended flavouring concentrates in any form are used; confectionery and chocolates; gramophones, including record players, and gramophone records; cinematograph films and projectors; photographic apparatus and goods; office machines and apparatus such as typewriters, calculating machines, cash registering machines, cheque writing machines, intercom machines and teleprinters; steel furniture, whether made partly or wholly of steel, safes, strong boxes, cash and deed boxes and strong room doors; latex foam sponge and polyurethane foam; crown corks, or other fittings of cork, rubber polyethylene or any other material; and pilfer-proof caps for packaging or other fittings of cork, rubber, polyethylene or any other material.

It will be seen that while the Eleventh Schedule does not contain items such as motor cars, airconditioners, mosaic tiles and glazed tiles, it contains items such as tooth powder, soap, and typewriters. This means that whereas individuals, Hindu

undivided families, and associations of persons investing in equity shares issued by public companies engaged in the production of motor cars, airconditioners, mosaic tiles, and glazed tiles are eligible to claim the tax benefit available under section 80CC, those investing in equity shares of public companies engaged in the production of tooth powder, soap, and typewriters will be ineligible for the benefit. There appears to be no justification for such discrimination.

One can go on giving examples of tax expenditure provisions which damage the equity of the tax system, make the tax system more complex, enlarge tax avoidance possibilities, or add to costs of tax administration. But the question which arises here is: What is it that should be done in order to control tax expenditures? This, in my view, is an important public policy question.

In order that tax expenditures are effectively controlled, it will be absolutely necessary to study in detail each of the tax expenditure provisions. When studying a tax expenditure provision, one will have to deal with questions such as: How much does this provision cost? Is the activity benefiting from this provision high on the national agenda? Is the tax route the better way of assisting this activity? Once the various tax expenditure provisions have been studied in this manner, one should be in a position to come up with a list of provisions which deserve to be eliminated.

One may ask: What can be expected to happen when things begin to improve on the front of tax expenditures in India? Firstly, the tax system will become much less complex. In my view, it will be impossible to bring about any meaningful simplification in India's tax system so long the country's policymakers and their advisors continue to believe in the proliferation of tax expenditures. The point to remember is: If you add to tax expenditures, you add to tax complexity.

Secondly, proper management of tax expenditures will help in restoring the confidence of the people in the tax system. The people seem to believe that the present tax system is unfair - in the sense that while the privileged groups escape the tax net by paying little or no tax, the average person must pay his taxes.

Finally, proper management of tax expenditures will also help government in mobilising additional resources. The importance of this for meeting the challenges which the country faces today can hardly be overemphasised.

Some people might argue that the Government of India is aware of the importance of proper management of tax expenditures and that it has already started doing the needful in the matter. In support of this, they may cite the budget of the Government of India presented by Finance Minister Pranab Kumar Mukherjee on February 28, 1983. While presenting this budget, the Finance

Minister said: "Our corporate tax structure is riddled with a large number of different kinds of deductions. While each deduction may seem to have a merit, the aggregate effect is to complicate tax administration, provide opportunities for misuse and reduce the growth of revenues. As a step towards rationalisation of this structure, I have reviewed the various deductions."[1] After having said this, the Finance Minister proposed the withdrawal of the following tax expenditures: export markets development allowance (section 35B); rural development allowance (section 35CC); deduction in respect of payment to associations and institutions for carrying out rural development programmes (section 35CCA); deduction in respect of profits and gains from business of livestock breeding, poultry and dairy farming (section 80JJ); deduction in respect of profits and gains from business of growing mushrooms (section 80JJA); and deduction in the case of an Indian company in respect of royalties, etc. received from any concern in India (section 80MM).

The Finance Minister also proposed levy of a minimum tax on companies making profits but paying no tax at all or only a nominal tax. This is what he said when making this proposal: "Hon'ble Members must be aware of the phenomenon of companies which are flourishing, but are paying no tax at all, or only a nominal tax. This is largely due to these companies availing of the tax incentives and concessions available under the provisions

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[1] Government of India: Finance Minister's Speech (Part B), Budget 1983-84 (February 28, 1983), p. 28.

of the Income-tax Act. It has been a matter of concern to us that under our tax system several highly profitable companies are able to reduce their tax liability to zero even though they continue to pay high dividends. It seems reasonable that profitable and prosperous companies should contribute at least a small portion of their profits to the national exchequer at a time when other and less better off sections of society are bearing a burden. I therefore propose to provide that fiscal incentives and concessions shall not absorb more than 70 per cent of the profits. This would secure that companies pay a minimum tax, on at least 30 per cent of their profits."[1]

Two months later, while moving the Finance Bill for consideration, the Finance Minister withdrew the proposals to drop sections 35CC and 80JJ. He justified the decision regarding section 35CC by saying: "It has been represented that some companies have been doing useful work in the field of rural development and the proposed withdrawal of rural development allowance would adversely affect such activity by the corporate sector. Having regard to the continued need for the involvement of the corporate sector in rural development, I propose to continue the existing provision relating to deduction in respect of expenditure directly incurred by companies and co-operative societies on approved programmes of

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[1]Ibid., p. 27.

rural development."[1] As regards section 80JJ, this is what he said: "The Bill seeks to withdraw the special deduction allowed in respect of profits and gains from business of livestock breeding or poultry or dairy farming. The agricultural community engaged in these activities has pointed out that withdrawal of this concession may particularly affect smaller business. As I find merit in this representation, I have decided to retain the existing concession for the time being."[2]

It may be noted that while, on the one hand, the Finance Minister has withdrawn some tax expenditures, he has introduced, on the other hand, the following tax expenditures: special provisions relating to taxation of income from certain specified assets in the case of non-resident Indian citizens and foreign nationals of Indian origin (section 115C); tax concession based on export turnover (section 80HHC); and deduction in respect of any sum paid by a tax-payer to the National Fund for Rural Development (section 80GGA). In addition, the Finance Minister has made a number of changes designed to restrict, extend or enlarge existing tax expenditures. Examples are: reduction in benefit available under the provision relating to agricultural development allowance (section 35C); extension of investment allowance benefit to new machinery and plant installed for the purposes of the business of carrying on repairs

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[1]See <u>The Hindustan Times</u> (New Delhi), April 28, 1983, p. 5.

[2]<u>Loc</u>. <u>cit</u>.

to ocean-going vessels or other powered craft (section 32A); and enlargement of tax benefit in respect of income from specified financial assets (section 80L).

What does one make out of all this? Can one say that the Government of India has really done something to improve the management of tax expenditures? The Government of India might be aware of the importance of proper management of tax expenditures but, in my view, it has not yet made any appreciable effort in this area. The Government has not even set up the infrastructure required for proper management of tax expenditures. The result is that it continues to take decisions concerning tax expenditures on the basis of grossly inadequate, sometimes even irrelevant, data.[1] This is not a happy state of affairs.

[1] Take, for instance, its proposal to withdraw the provision relating to rural development allowance (section 35CC). It announced the proposal without knowing the whole story of this tax expenditure provision: the amount of deductions allowed under this provision; the tax effect of these deductions; the number of assessments in which deductions under this provision were allowed; the impact of this provision on rural development; details of misuse, if any, of this provision; difficulties experienced by the Income Tax Department in operating this provision; and so on.

IV. TAX BURDEN ON THE RURAL NON-POOR[1]

We have presented earlier in this study our estimates of tax burden on different consumption expenditure groups in the rural and the urban sectors in India. Two points emerge from a careful examination of these estimates. The first point relates to tax burden on the rural people. They pay taxes at the rate of 10.12 per cent of their consumption expenditure (11.30 per cent under Variant B).[2] Considering that the rural people account for nearly three-fourths of the total consumption expenditure in the country, the taxes paid by them add up to quite a sizeable proportion of the total taxes people in India pay. According to our calculations, this proportion works out to nearly 44 per cent (nearly 50 per cent under Variant B). The point to note is that the share of the rural people in the total tax burden is not as low as it is generally believed to be.

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[1] This section draws upon my "Taxation and Subsidies" in: Indian Society of Agricultural Economics: Indian Agricultural Development (forthcoming).

[2] As stated earlier, we have classified the incidence assumptions used for estimating tax burden on different consumption expenditure groups into two variants, Variant A and Variant B. Variant A treats corporation tax and export duty as direct taxes and, therefore, assumes that their incidence is not shifted. In contrast, Variant B treats both the taxes as indirect taxes and assumes that their incidence is shifted forward in the form of higher product prices. The treatment of all other taxes is the same in both Variant A and Variant B.

The second point relates to equity in taxation as between the rural and the urban sectors.[1] The data clearly show that tax burden on the urban people is much higher than that on the rural people. But what is to be noted is that a good part of the rural-urban disparity in tax burden is due to the disparity in tax burden on the highest consumption expenditure groups (Rs. 100 and above) in the two sectors. One can also see a disparity in tax burden on the lower consumption expenditure groups in the two sectors, but it is of a much lower order. It is not due to any formal bias of the tax system in favour of the lower consumption expenditure groups in the rural areas and can largely be explained in terms of the rural-urban differences in the relative shares of cash and non-cash expenditures in total consumption expenditures, with the ratio of cash purchases to total consumption expenditures for the same expenditure groups being lower in the rural sector than in the urban sector.[2]

The disparity in tax burden in the highest consumption expenditure groups is such that whereas the tax burden on the highest consumption expenditure group in the urban sector works out to be of the order of 86.60 per cent (71.40 per cent under

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[1]What holds true of equity in taxation as between the rural and urban sectors, by and large also holds true of equity in taxation as between the agricultural and non-agricultural sectors.

[2]As things stand, it is only the cash expenditures which are subject to incidence of taxes.

Variant B), that on the highest consumption expenditure group in the rural sector comes to only 19.68 per cent (22.02 per cent under Variant B). Two factors are responsible for such a disparity in tax burden. Firstly, the burden of indirect taxes (e.g. central excise duty, import duty, sales tax) on the highest consumption expenditure group in the rural sector is appreciably lower than that on the highest consumption expenditure group in the urban sector. This is a fact which has been clearly brought out in a number of tax incidence studies, including those undertaken commissioned by the Taxation Enquiry Commission,[1] the Union Ministry of Finance,[2,3] and the Indirect Taxation Enquiry Committee.[4] But the point which needs to be noted here is that the relatively low incidence of indirect taxes on the highest consumption expenditure group in the rural sector is not due to any formal

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[1] Government of India, Ministry of Finance: Report of the Taxation Enquiry Commission 1953-54, vol. I (Delhi, Manager of Publications, 1955), pp. 68-69.

[2] Government of India, Ministry of Finance: Incidence of Indirect Taxation, 1958-59 (New Delhi, 1961), statement II.

[3] Government of India, Ministry of Finance: Incidence of Indirect Taxation, 1963-64 (New Delhi, 1969), table VI.

[4] Government of India, Ministry of Finance: Report of the Indirect Taxation Enquiry Committee, part II (1978), p. 90.

bias of the system of indirect taxation in the country in favour of this group. As things stand, it is largely due to differences in the consumption patterns of the top rural and urban consumption expenditure groups and the failure of the tax system to adapt itself to these differences.

And secondly, the burden of direct taxes on the higher strata in the agricultural sector is considerably lower than that on the comparable strata in the non-agricultural sector. This fact has also been clearly brought out.[1]

As things stand now, there is no wealth tax on agricultural property. There used to be a levy of wealth tax on agricultural property, but it has been discontinued. The decision to this effect was announced by the Finance Minister when presenting the budgets of the Government of India for 1980-81 and 1982-83. This is what the Finance Minister said when presenting the budget of the Government of India for 1980-81: "At present, agricultural property is included in the taxable wealth for the purposes of the levy of wealth-tax. At the time when agricultural property was brought within the tax net, it was hoped that it would be a potent instrument for mobilising resources from the affluent section of agriculturists.

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[1]See: Government of India, Ministry of Finance: Report of the Committee on Taxation of Agricultural Wealth and Income (1972).

But our experience of over the last decade has been most disappointing. The amount realised as wealth tax on agricultural property has generally been less than Rs. 1 crore per annum. The valuation of agricultural land has posed difficulties leading to complaints of harassment. As this tax has clearly failed to achieve its original objective, I propose to discontinue the levy of wealth-tax on agricultural property except in the case of owners of tea, coffee, rubber and cardamom plantations. I am sure that this measure will be widely welcomed by our farmers."[1] And this is what the Finance Minister said when presenting the budget of the Government of India for 1982-83: "While the levy of wealth-tax on agricultural property was discontinued by the Finance (No. 2) Act, 1980, owners of tea, coffee, rubber and cardamom plantations continue to be chargeable to wealth-tax. Our experience is that the valuation of agricultural land forming part of such plantations leads to administrative difficulties, complaints of harassment and litigation. The yield from this levy is also insignificant. I, therefore, propose to discontinue the levy of wealth-tax on such plantations as well."[2]

The Finance Minister has also decided to discontinue the levy of estate duty on agricultural land. This is what he said when

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[1]Government of India: Finance Minister's Speech (Part B), Budget 1980-82 (June 18, 1980), p. 22.

[2]Government of India: Finance Minister's Speech (Part B), Budget 1982-83 (February 27, 1982), pp. 29-30.

presenting the budget of the Government of India for 1983-84: "Our experience is that the valuation of agricultural land leads to administrative difficulties and litigation. The yield from this levy has also not been significant over the past several years. Moreover, after the abolition of wealth-tax on agricultural land, including plantations, there is little practical justification for continuing the levy of estate duty on agricultural land. I, therefore, propose to remove the levy of estate duty on agricultural land."[1]

This does not mean that now there is no tax on agricultural property. The tax system includes a tax, called land revenue, which is leviable by the states and union territories. But in terms of collections, land revenue is a weak tax (Table 6); in terms of incidence, it is "at best a proportional tax."[2]

The agricultural sector also bears the incidence of stamp duties and registration fees. The revenue from these taxes amounted to Rs. 277.9 million in 1950-51, Rs. 472.2 million in 1960-61, Rs. 1,348.9 million in 1970-71 and Rs. 4,363.5 million in 1980-81. The incidence of these taxes falls mainly on property owners, including those owning agricultural property. Data on the share of the agricultural sector in the revenue from these taxes are not available. But if

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[1]Government of India: Finance Minister's Speech (Part B), Budget 1983-84 (February 28, 1983), p. 33.

[2]Government of Uttar Pradesh, Finance Department: Uttar Pradesh Taxation Enquiry Committee Report 1974 (Lucknow, 1975), p. 107.

TABLE 6

COLLECTIONS FROM AGRICULTURAL INCOME TAX AND LAND REVENUE

(Rs. million)

Year	Collections from agri-cultural income tax	Collections from land revenue	Collections from agricultural in-come tax as per cent of total tax collections of the centre, states & union territories	Collections from land revenue as per cent of total tax collections of the centre, states and union territories
1	2	3	4	5
1950-51	35.9	515.7	0.57	8.23
1955-56	76.8	788.9	1.00	10.28
1960-61	97.1	977.8	0.72	7.24
1965-66	99.1	1,201.8	0.34	4.11
1970-71	105.3	1,208.2	0.22	2.54
1971-72	129.0	1,022.1	0.23	1.83
1972-73	122.6	946.0	0.19	1.47
1973-74	118.2	1,595.3	0.16	2.16
1974-75	138.9	1,623.6	0.15	1.76
1975-76	284.8	2,341.0	0.25	2,09
1976-77	345.5	1,874.9	0.28	1.52
1977-78	619.6	1,785.4	0.47	1.35
1978-79	803.8	2,014.3	0.52	1.30
1979-80	583.6	1,648.6	0.33	0.93
1980-81	464.0	1,568.5	0.23	0.79
1981-82(RE)	411.3	2,092.1	0.17	0.88
1982-83(BE)	455.8	2,213.3	0.17	0.80

Source: Ministry of Finance, Government of India.

one goes by the estimate adopted by the Uttar Pradesh Taxation Enquiry Committee, it won't be higher than 20 per cent.

It is not just agricultural property which is subjected to taxes. Agricultural income is also subjected to taxation. The tax system includes a tax, called agricultural income tax, which is leviable by the states and union territories. Most of the revenue collected under this head comes only from plantations. The rate of agricultural income tax on plantation companies varies from 65 per cent in Kerala and Tamil Nadu to 75 per cent in Assam and West Bengal, which is higher than the rate of central income tax on industrial companies. But, unfortunately, yieldwise, agricultural income tax is a very weak tax (see Table 6).

Apart from state agricultural income tax, agricultural income is assessable under central income tax. In terms of rule 8 of the central income tax rules, out of every Rs. 100 income derived by a taxpayer from the business of sale of tea grown or manufactured by him in India, Rs. 40 is regarded as business income, assessable to central income tax, and Rs. 60 is deemed to be agricultural income, assessable to state agricultural income tax. One would expect that in no case would more than 100 per cent of the profit earned be liable to tax. But this is not so. The states of West Bengal and Kerala have recently passed legislations purporting to charge the entire Rs. 100 to state agricultural income tax instead of only Rs. 60. Some taxpayers are contesting this by

filing writ petitions in the Supreme Court of India, but in the meantime, since the central government has not abandoned its claim for tax on Rs. 40, they face an aggregate demand for tax on 140 per cent of their incomes. This does not happen to incomes in the non-agricultural sector. This, one can say, is a clear case of horizontal inequity in income taxation, with the agricultural sector being at a disadvantage compared to the non-agricultural sector.

Further, in terms of a provision introduced in 1973, net agricultural income of individuals, Hindu undivided families, unregistered firms, association of persons, bodies of individuals and artificial juridicial persons is taken into account for determining the rate of central income tax applicable to non-agricultural income. This takes effect only if a taxpayer has taxable non-agricultural income exceeding the minimum exemption limit. In determining the rate of tax on non-agricultural income, the agricultural income and non-agricultural income are combined in the following manner and order: (i) the initial exemption allowed out of non-agricultural income; (ii) agricultural income; and (iii) balance of non-agricultural income. As regards the amount of income tax payable by a taxpayer, it is calculated in the following manner: (i) the agricultural and non-agricultural components of a taxpayer's income are first aggregated and income tax calculated on the aggregate as if such aggregate is the total income; (ii) income tax is then calculated on the net agricultural income as increased by an amount equal to the initial

exemption, as if such increased net agricultural income is the total income; (iii) the amount by which the income tax calculated under (i) exceeds the amount calculated under (ii) is the income tax payable by the taxpayer. Thus, if an individual earns during the financial year 1983-84 an agricultural income of Rs. 25,000 and a non-agricultural income of equal amount, he will be liable to pay income tax of Rs. 4,500. If his non-agricultural income is Rs. 25,000 and he earns nothing as agricultural income, his income tax liability will amount to Rs. 3,094. On the other hand, if his non-agricultural income is Rs. 50,000 and he earns nothing as agricultural income, he will be liable to pay income tax of Rs. 14,063.

This means that the provision introduced in 1973 has the effect of indirectly taxing agricultural income when a taxpayer has, in addition to agricultural income, taxable non-agricultural income exceeding the exemption limit. (The exemption limit presently in force in the case of individuals, Hindu undivided families (other than those with one or more members having separate income exceeding the exemption limit), unregistered firms, associations of persons, etc., is Rs. 15,000.) But the point to be noted is that the rate of tax applicable to agricultural income, as can be gathered from the above illustration, is much lower compared to that applicable to non-agricultural income.

The total revenue from central income tax now amounts to about Rs. 40,000 million. Data on revenue from central income tax

attributable to agricultural incomes are not available, but discussion with knowledgeable people suggests that it is pitifully low.

A number of suggestions for reforming the system of agricultural taxation in India have been made. One of these suggestions has attracted considerable attention. This relates to the scheme of agricultural holdings tax (AHT). The scheme was suggested by the Committee on Taxation of Agricultural Wealth and Income, headed by K N Raj. The AHT is designed to replace the existing system of land revenue and related surcharges and cesses. Its focus is on rationalisation of taxation of agricultural lands. The main features of the scheme of AHT are: (a) the country should be divided into a sufficiently large number of soil-climatically homogenous districts/tracts so that differences having any significant influence on productivity are taken into account; (b) for each such district/tract norms of output of different crops per hectare for each year should be worked out on the basis of estimates of yield for the previous ten years; (c) the output so estimated should be valued at the relevant average harvest prices of the preceeding three years; (d) from the value of the gross output of the crops so arrived at, allowance should be made for the paid-out costs of cultivation other than irrigation expenses; (e) for each district/tract, there will thus be a schedule of rateable value of land per hectare under different crops/crop-groups. The schedule should be revised every year, taking into account any revision that may be made from time to time in the scale of deductions to be made on account of the costs of cultivation of

different crops, and included in the legislation of the year in question; (f) the rateable value of an agricultural holding will be computed from the rateable values of lands coming under it, after deducting the expenses of irrigation. To provide for the costs of development, a development allowance should be given to all agricultural holdings at the rate of 20 per cent of rateable value, subject to a maximum of Rs. 1,000; and (g) the actual AHT liability would be arrived at by applying a simple formula to the taxable rateable value of the aggregate operational holding of a family. For example, if the taxable rateable value of a holding is Rs. 9,000, the AHT liability would be 9.0/2, or 4.5 per cent of Rs. 9,000 which is equal to Rs. 405.

The Committee felt that the AHT would be free from the deficiencies of the existing land revenue system, namely: wide disparity in incidence as between different regions and even between areas within a region, lack of progressivity and lack of revenue elasticity. It was estimated that the AHT would yield an additional revenue of Rs. 1,500 million per annum if applied to holdings with rateable value of Rs. 5,000 or above. The yield, it was felt, would be larger, possibly around Rs. 2,000 million, if it was extended to all holdings with rateable value of Rs. 2,500 or more.[1]

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[1]Government of India, Ministry of Finance: Report of the Committee on Taxation of Agricultural Wealth and Income (1972).

Although the states were consulted by the Committee while formulating its recommendations, practically none of them has adopted the AHT.[1] Amaresh Bagchi, who functioned as a full-time adviser to the Committee, feels that "the principal consideration which disuaded the states from implementing the AHT seems to be that it would involve insuperable administrative problems. What may have made the AHT look so formidable are the requirements of: (i) drawing up of schedules of rateable value of land for each homogenous district/tract separately for each major crop/crop-group grown in each such district/tract; (ii) revision of the schedules of rateable value of land every year; (iii) annual assessment of each holding on the basis of crops grown every year; and (iv) aggregation of holdings on operational basis."[2]

The scheme of AHT was considered in the Planning Commission in March 1973. The consensus of opinion was that the scheme involved administrative and legal complexities and might be difficult to implement. The Ministry of Agriculture, Government of India, also did not favour immediate introduction of the scheme, but preferred a simple system of raising resources from agriculture till such time as the states had built up elaborate administrative arrangements necessary for levying the AHT.[3]

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[1] The government of Haryana after considering the report of the Committee on Taxation of Agricultural Wealth and Income, introduced a progressive land holdings tax with effect from June 16, 1973. But this tax is not quite on the lines suggested by the Committee.

[2] Amaresh Bagchi: "Agricultural Holdings Tax: A Modified Scheme", Economic and Political Weekly, September 23, 1978, p. 1633.

[3] Lok Sabha Secretariat: 147th Report of the Public Accounts Committee (1978-79), Sixth Lok Sabha (New Delhi).

Recently, the matter was considered by the Gujarat Taxation Enquiry Commission. The Commission felt that introduction of the AHT as suggested by the Committee on Taxation of Agricultural Wealth and Income "would involve complex procedures and throw up formidable administrative problems, legal complexities and that it might be difficult to implement."[1] The Commission also felt that the AHT "might not lead to any substantial increase in revenue."[2] Accordingly, the Commission did not favour the introduction of AHT in Gujarat.

Bagchi believes that it is possible to come up with a scheme of AHT which provides an expeditious and not too exacting method of land revenue revision. Indeed, he has put forward a modified scheme of AHT which he believes would "suit the administrative resources of the state governments ... and help to secure additional revenue of the order of Rs. 300 crore in the immediate future."[3] The modifications suggested by him are: (a) the AHT assessments once made may be kept for a period of, say, five years; (b) the schedules of rateable value of land per hectare may be revised once every five years or so; (c) the rateable value of land in a given homogenous area/tract may be determined on the basis of the average gross value of output of only one or two crops; (d) the norms of output

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[1] Government of Gujarat: <u>Report of the Gujarat Taxation Enquiry Commission</u> (Gandhinagar, 1980), p. 31.

[2] Ibid, p. 33.

[3] Amaresh Bagchi, op. cit., p. 1642.

may be fixed on the basis of averages of output for five years, while the prices to be used may be the averages of three or four years; and (e) the tax may be assessed on the basis of ownership holdings.

Lakdawala has suggested the levy of a tax "based on potential income, which will be judged from the type of soil, within a homogenous tract, with reference to the crops usually grown on it. Wet and dry land will have to be separately assessed ... The type of crops on each type of soil will also have to be obtained by enquiry, and expenditure on each crop within certain narrow limits, say 45-55 per cent, decided. The yield of each crop will be decided on the basis of a sufficient number of crop-cutting experiments ... Prices have increased rapidly and a substantial decline in them is ruled out, so that a three years' price average may suffice. To avoid complications, it should not be necessary to make recalculations every year. Calculations will have to be done at the time of land resettlement which should be done only every ten years ... The rates may vary from 2 per cent at the lowest to 20-30 per cent maximum."[1] Lakdawala believes that his scheme of tax on potential income will "make the rural tax system more progressive and the rural areas more self-reliant."[2]

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[1] D.T. Lakdawala: "Direct Taxation on Agriculture", in Indian Journal of Agricultural Economics, October-December 1975, p. 14.

[2] Lakdawala, loc. cit.

There have been some other suggestions such as levy of an agricultural income tax. It is believed by many scholars that if we have an agricultural income tax patterned on the non-agricultural income tax, then there will be no talk of inequity in taxation as between the agricultural and non-agricultural sectors. As things stand now (1983-84), an individual earning non-agricultural income is liable to pay income tax when his annual income exceeds Rs. 15,000, and the marginal tax rate increases progressively with the size of the taxable income, reaching a maximum of 67.5 per cent (including surcharge) at levels of income exceeding Rs. 100,000. Thus, if an individual makes an income of Rs. 20,000, his income tax liability amounts to Rs. 1,406. But in case he makes an income of, say, Rs. 1,20,000, he ends up paying as much as Rs. 58,078 by way of income tax.[1] But the story is entirely different when it comes to tax on agricultural incomes. In terms of section 10(1) of the Income Tax Act, agricultural income is exempt from tax. Under the Constitution of India, the power to tax agricultural income vests exclusively with the states. And the states, as is well known, have not done much to tax agricultural incomes.

To conclude this section, the tax burden on the rural non-poor is much less than that on the urban non-poor. There is no dearth of sensible suggestions for taking care of this inequity.

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[1]On account of numerous provisions in the Income Tax Act, 1961 (e.g., sections 80C, 80CC, 80L), the actual progression is much less steep than the nominal rate structure suggests. A significant element of progression nevertheless remains.

One hopes the policymakers will make up their mind soon so that the tax system may be able to raise larger resources from the rural non-poor.

V. GOVERNMENT EXPENDITURES AND THE POOR

Government expenditures in India have grown from Rs. 8,604.7 million in 1950-51 to Rs. 22,479.9 million in 1960-61, Rs. 70,497.1 million in 1970-71, Rs. 304,229.9 million in 1980-81, Rs. 352,881.7 million in 1981-82 (revised estimates) and to Rs. 392,589.1 million in 1982-83 (budget estimates).[1] Of course, not all of this increase can be regarded as real - a part of it has been due to the rise in prices. But even if an adjustment is made to account for the rise in prices, the fact would remain that an increase of considerable magnitude has taken place in the size of government expenditures in India since the beginning of the fifties.

That government expenditures have recorded an impressive growth in India will become clearer if one analyses them in relation to national income: The percentage of government expenditures to

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[1] These figures represent combined expenditures of the central, state and union territory governments. Expenditures include all non-repayable payments whether requited or unrequited, and whether for current or capital purposes.

national income has moved up from a mere 9.74 per cent in 1950-51 to 16.95 per cent in 1960-61, 20.59 per cent in 1970-71, 28.56 per cent in 1980-81, 29.11 per cent in 1981-82, and to 30.88 per cent in 1982-83.

A striking feature of growth in government expenditure in India is that it has not been of a uniform nature. Indeed, it has been quite unevenly distributed, not only over time but also over the various purposes or functions. Take, for example, the expenditure on economic services and that on community and social services. While government expenditure on both the services has grown, that an economic services has grown at a much faster rate. Indeed, government expenditure on economic services has grown so fast that it now accounts for about one-third of the total government expenditure, as against only about one-sixth in 1950-51. As regards the community and social services, the position is that while government expenditure on them has also grown, their relative importance has suffered on erosion: Their share in total government expenditure has declined from about 36 per cent to about 29 per cent.

But what is important to note is that not all community and social services have suffered erosion in their relative importance. Indeed, some community and social services have even recorded an improvement in their importance. Education is a case in point. The share of government expenditure on education in total government expenditure has grown from less than one-thirteenth in 1950-51 and about one-tenth in 1960-61 to about one-eighth in 1982-83.

A word may now be said about general public services. Government expenditures under this category are incurred for the provision of the basic administrative structure of the nation. Thus expenses on general administration, tax collection, police, currency and mint, conduct of external relations and defence are included under the category of general public services. As things stand now, these services account for about one-fourth of the total government expenditures. This is markedly smaller than what it used to be in, say, the early fifties. But if viewed in relation to national income, we find that government expenditure on general public services has grown from less than four per cent in the early fifties to over seven per cent now.

It may be noted that defence services account for over one-half of the total expenditure on general public services. Expenditure on defence services has grown from Rs. 1,683.2 million in 1950-51 to Rs. 2,899.3 million in 1960-61, Rs. 12,387.4 million in 1970-71, Rs. 38,935.3 million in 1980-81, Rs. 48,419.7 million in 1981-82, and to Rs. 55,509.8 million in 1982-83.

There are certain government expenditures which do not fall into any of the three functional categories of government expenditures (viz. economic services, community and social services and general public services). These expenditures are: interest payments, compensation and assignments to local bodies, etc., and compensation to land holders. The total outgo on account of

these items has grown from Rs. 723.6 million in 1950-51, Rs. 2,316.1 million in 1960-61, Rs. 7,516.4 million in 1970-71, Rs. 31,821.7 million in 1980-81, Rs. 41,085.3 million in 1981-82, and to Rs. 47,672.5 million in 1982-83. These expenditures now account for 12.14 per cent of all government expenditures, as against 8.41 per cent in 1950-51 and 10.30 per cent in 1960-61.

Let us now look at the economic mix of government expenditures. That is, let us see how much of government expenditure in India is incurred on wages and salaries, how much on interest, how much on subsidies, and so on.

Wage and salary payments to government employees

A lot of expenditure is incurred by the central, state and union territory governments on their employees. The heads under which this expenditure is generally incurred are: wages and salaries (including various allowances), pensions and other retirement benefits, housing facility, leave travel concessions, educational facilities and allowances, medical facilities, staff amenities, etc. Wages and salaries account for the largest share of expenditure on government employees.

There has been considerable increase in the number of central, state and union territory government employees in India. The figure which stood at 5.10 millions in March 1961, rose to 6.36 millions in March 1966, 6.92 millions in March 1971, 7.99 millions in March 1976, and to 8.95 millions in March 1981.

The six states of Bihar, Madhya Pradesh, Maharashtra, Tamil Nadu, Uttar Pradesh and West Bengal alone account for over one-half of the total government employees in the country. The state of Uttar Pradesh has the highest number of government employees. While, on the whole, state/union territory government employees are more numerous than the central government employees, the latter are more numerous than the former in Delhi, Maharashtra, Meghalaya and West Bengal. The state of Maharashtra has the highest number of central government employees.

No state and union territory-wise data are available on wage and salary payments to government employees. The Central Statistical Organisation publishes regularly the figure relating to expenditure on wages and salaries to people employed in government administrative departments all over the country. But no break-up of this figure is available. The Seventh Finance Commission made an attempt to collect detailed data on expenditure incurred by the state governments on salaries and allowances of their employees. It seems the Commission got the data, but, unfortunately, it was not able to publish it.

The central government and many state and union territory governments analyse regularly the various government transactions and publish economic/economic-cum-functional classifications of their budgets. They also conduct censuses of their employees and publish the results. The economic/economic-cum-functional

classifications of the government budgets and the census reports contain some useful data. We have made use of these data and have come up with estimates of the expenditure on wages and salaries of government employees. Table 7 presents these estimates.

On the basis of the data presented in Table 7, one can say that wage and salary payments account for about one-fourth of all government expenditures in India.[1] One can also say that the state and union territory governments, taken together, spend more on wages and salaries than the central government does.

The data in Table 7 also throw light on the relationship between the expenditure on wages and salaries and the amount of taxes raised. Even if one treats the hill states of Himachal Pradesh, Jammu and Kashmir, Manipur, Meghalaya, Nagaland, Sikkim and Tripura and all the union territories as special cases, one discovers that in a number of states expenditure on wages and salaries of government employees accounts for a very high proportion of the total taxes raised. So much so, in the case of Orissa, the expenditure on wages and salaries of Orissa government employees works out to be higher than the taxes raised by the Government of Orissa. In Kerala, Madhya Pradesh and Rajasthan, the wage and salary payments to state government employees account for over three-fourths of the

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[1]The share of expenditure on wages and salaries would be still higher if account is taken of semi-government employees, such as those employed by zilla parishads, municipalities and government-aided educational institutions.

TABLE 7

WAGE AND SALARY PAYMENT TO GOVERNMENT EMPLOYEES

1975-76

	Total expenditure (Rs. million)	Total taxes raised (Rs. million)	Expenditure on wages and salaries (Rs. million)	Expenditure on wages and salaries as per cent of total expenditure	Expenditure on wages and salaries as per cent of total taxes raised
1	2	3	4	5	6
I. Central government	79,386.6	76,087.8	15,141.8	19.07	19.90
II. State governments:					
Andhra Pradesh	5,918.3	3,255.5	1,537.2	25.97	47.22
Assam	1,873.3	593.3	351.1 1/	18.74	59.18
Bihar	4,536.3	1,863.6	1,206.8 2/	26.60	64.76
Gujarat	4,054.8	2,359.9	703.9	17.36	29.83
Haryana	1,623.5	1,169.4	749.9	46.19	64.13
Himachal Pradesh	880.4	157.6	439.8	49.95	279.06
Jammu & Kashmir	1,740.4	253.0	728.1 3/	41.84	287.79
Karnataka	4,049.5	2,367.3	1,427.7	35.26	60.31
Kerala	3,674.8	1,597.1	1,249.3 4/	34.00	78.22
Madhya Pradesh	4,303.2	2,313.8	1,947.6	44.43	84.17
Maharashtra	8,656.5	5,859.6	1,554.3	17.96	26.53
Manipur	373.9	19.4	123.2	32.95	635.05
Meghalaya	323.8	21.8	68.3	21.09	313.30
Nagaland	514.1	21.9	191.7 2/	37.29	875.34
Orissa	2,839.7	684.1	894.3	31.49	130.73
Punjab	2,577.5	1,728.0	1,158.9	44.96	67.07

	1	2	3	4	5	6
	Rajasthan	3,606.9	1,308.0	1,272.9	35.29	97.32
	Sikkim	100.4	11.4	17.9[5/]	17.83	157.02
	Tamil Nadu	5,533.8	3,190.9	1,561.8	28.22	48.95
	Tripura	393.8	17.6	221.9[2/]	56.35	1260.80
	Uttar Pradesh	8,276.3	3,933.6	2,418.0	29.22	61.47
	West Bengal	5,430.4	2,829.6	1,528.1	28.14	54.00
III.	Union Territories:					
	Arunachal Pradesh	239.0	0.9	47.8	20.00	5311.11
	Goa, Daman & Diu	334.2	94.1	118.7	35.52	126.14
	Mizoram	332.7	2.2	61.3[5/]	18.43	2786.36
	Pondicherry	158.6	75.9	81.7	51.51	107.64
IV.	All India	151,812.7	111,817.3	36,804.0	24.24	32.91

Notes: 1/ The Government of Assam does not publish any economic and functional classification of its budgets. As regards the census of Assam government employees, the latest available census relates to the employees as on March 31, 1973. The total wage and salary bill for 1972-73 was computed by using the data in this census. Assuming that the proportion of wage and salary payments in total revenue expenditure remained unchanged between 1972-73 and 1975-76, we obtained the figure for 1975-76.

2/ The Government of Bihar, Nagaland and Tripura do not publish any economic and functional classification of their budgets. As regards the census of their employees, the latest available censuses relate to the employees as on March 31, 1971 (March 31, 1970 in the case of Tripura). The methodology used for estimating the 1975-76 wage and salary payments by these governments is similar to that used in the case of Assam.

3/ The Government of Jammu and Kashmir does not publish any economic and functional classification of its budgets. Nor has it undertaken any census of its employees. We have estimated the wage and salary payments to Jammu and Kashmir government employees by assuming that the ratio of wage and salary payments to revenue expenditure in Himachal Pradesh holds good for Jammu and Kashmir also.

4/ The Government of Kerala publishes data on salary bill of the state government in its Kerala Budget in Brief (annual).

5/ With no required data available in respect of the state of Sikkim and the union territory of Mizoram, the figures have been estimated by assuming that the proportion of wage and salary payments to Sikkim/Mizoram government employees in total revenue expenditure in Sikkim/Mizoram is the same as in Assam.

Sources: For columns 2-3 : Budget documents of the central, state and union territory governments.

For column 4 : Reports on census of government employees and economic and functional classification of budgets issued by the central, state and union territory governments.

taxes raised. This, in a way, indicates the extent to which states depend on transfers by the central government for financing their expenditures.

Interest payments

Interest payments have grown from Rs. 711.8 million in 1950-51 to Rs. 2,175.6 million in 1960-61, Rs. 7,465 million in 1970-71, Rs. 29,565.9 million in 1980-81, Rs. 38,432 million in 1981-82, and to Rs. 44,599.8 million in 1982-83. It may be noted that interest payments now account for 11.36 per cent of all government expenditures in India, as against 8.27 per cent in 1950-51, 9.68 per cent in 1960-61, and 10.59 per cent in 1970-71.

Expenditure on subsidies

Subsidies galore in India. All governments give them. Some of the subsidies are open, others are hidden. Some involve budgetary outgo, others do not.

Unfortunately, the data on subsidies are not in a good shape. Take, for example, the data relating to 1975-76. According to the Central Statistical Organization (CSO), the budgetary subsidies given by the central and state governments amounted to Rs. 8,650 million in 1975-76.[1] Of this, agriculture, forestry, fishing and

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[1] Government of India, Ministry of Planning, Central Statistical Organisation: National Accounts Statistics 1970-71 - 1976-77 (New Delhi, 1979), Statement 23.

hunting accounted for Rs. 5,120 million; mining, manufacturing and construction, Rs. 780 million; economic services: general administration, regulation and research, Rs. 620 million; electricity, gas, steam and water, Rs. 320 million; transport and communication, Rs. 90 million; other economic services, Rs. 1,560 million; social security and welfare services, Rs. 130 million; housing and other community amenities, Rs. 10 million; and general administration, external affairs, public order and safety, Rs. 20 million. No other details are available. The CSO data do not even tell how much of the subsidies were given by the central government and how much by the state governments.

The central government and a number of state and union territory governments publish documents giving economic/economic and functional classifications of their budgets. We have put together all the data on subsidies available in these documents (see Table 8). A careful examination reveals that the data on subsidies compiled by the central and state governments do not tally with those compiled by the CSO, even though the data sources used by all of them are the same (viz., the demands for grants of the various ministries/departments). To illustrate, let us take the case of subsidies to industry. According to the central government data, these amounted to Rs. 2,156 million in 1975-76.[1] Subsidies to industry were also given by state governments (e.g., Government of Tamil Nadu gave a

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[1]Government of India, Ministry of Finance: An Economic and Functional Classification of the Central Government Budget 1977-78 (New Delhi, 1977), pp. 14-15.

TABLE 8

GOVERNMENT EXPENDITURE ON SUBSIDIES

1975-76

(Rs. millions)

	General services other than Defence	Education	Medical and public health	Other social services	Agriculture	Industry	Transport and communications	Other economic services	Unallocable	Total
1	2	3	4	5	6	7	8	9	10	11
Central government	1.0		6.0	1.0	4.0	2156.0	27.0	1.0	2501.0	4697.0
Andhra Pradesh 11/										
Assam 11/										
Bihar 11/										
Gujarat	31.3			0.4	210.5 1/	4.8				247.0
Haryana	0.1			2.4 2/	10.8	3.8		1.8		18.9
Himachal Pradesh										19.1
Jammu & Kashmir 11/										
Karnataka										20.6
Kerala 11/										
Madhya Pradesh					19.3	4.1		56.0 3/		79.4
Maharashtra		1.6	1.3	71.7 4/	133.8 5/	17.8	0.1	648.9 6/		875.2
Manipur 11/										
Meghalaya 11/										
Nagaland 11/										

1	2	3	4	5	6	7	8	9	10	11
Orissa				3.6 7/	7.7			16.0		27.3
Punjab					134.4 8/	6.2 9/				140.6
Rajasthan										31.5
Sikkim 11/										
Tamil Nadu			0.6	15.6 10/	2.6	28.4		3.0		50.2
Tripura 11/										
Uttar Pradesh				0.2	582.1	21.3				603.6
West Bengal					23.6			135.0		158.6
Arunachal Pradesh 11/										
Goa, Daman & Diu										0.4
Mizoram 11/										
Pondicherry										1.2

1/ Includes Rs. 206.5 million on account of imputed value of loss sustained by irrigation.

2/ The break-up is as follows: Social security and welfare services, Rs. 1.7 million; housing and other community amenities, Rs. 0.4 million; cultural, recreational and other religious services, Rs. 0.3 million.

3/ Rebates to electricity, gas, steam and water.

4/ The break-up is as follows: Housing and urban development, Rs. 70.1 million; other community services, Rs. 1.6 million.

5/ Includes trading losses of Rs. 100.4 million.

6/ The break-up is as follows: Water and power development, Rs. 140.9 million; trading losses, Rs. 505.6 million; other economic services, Rs. 2.4 million.

7/ Relates to social security and welfare services.

8/ The break-up is as follows: agriculture, Rs. 8.3 million; soil and water conservation, Rs. 0.4 million; food and nutrition, Rs. 124.0 million; animal husbandry, Rs. 0.9 million; dairy development, Rs. 0.8 million.

9/ The break-up is as follows: large and medium industries, Rs. 0.7 million; village and small industries, Rs. 5.5 million.

10/ The break-up is as follows: housing and urban development, Rs. 0.1 million; social security and welfare, Rs. 4.7 million; other social and community services, Rs. 10.8 million.

11/ No data on subsidies are available.

Source: Compiled by the author from data in various government documents giving economic/economic and functional classification of government budgets.

subsidy of Rs. 28.4 million[1]). But according to the CSO data, total subsidies to industry in 1975-76 amounted to just Rs. 780 million!

The subject of subsidies was studied recently by the Committee on Controls and Subsidies (Chairman : Vadilal Dagli) appointed by the Government of India. According to the data compiled by the Committee, the subsidies given by the central government in 1975-76 amounted to Rs. 7,120 million, 51.6 per cent higher than the estimate of the central government. According to the Committee, many of the items regarded as grants-in-aid or assistance by the central government are really of the nature of subsidies. Likewise, there are a number of items which are shown as subsidies, but which are really not of the nature of subsidies.[2] If proper adjustments are made to take care of such changes, the total amount of subsidies given by the central government can be estimated at Rs. 8,892 million. This is as much as 89.3 per cent higher than the estimate of the central government.

The Committee did not examine the issue relating to budgetary subsidies given by the various state and union territory governments. Our feeling is that the extent of underestimation in the case of

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[1]Government of Tamil Nadu, An Economic-cum-Functional Classification of the Tamil Nadu Government Budgetary Transactions 1977-78 (Madras, 1977), pp. 4-5.

[2]Government of India, Ministry of Finance: Report of the Committee on Controls and Subsidies - Annexes (New Delhi, 1979), pp. 90-106.

state and union territory subsidies may be higher than that in the case of central subsidies. Take, for example, the case of Rajasthan. According to the data compiled by the Government of Rajasthan's Directorate of Economics and Statistics, the total subsidies given by the Government of Rajasthan in 1975-76 amounted to Rs. 31.5 million,[1] which works out to just 0.9 per cent of its total expenditure in that year. When this was brought to the notice of the Government's Finance Secretary, he readily agreed that the figure was a gross underestimate.

One thing emerges from the foregoing discussion: the subsidies actually given by the central, state and union territory governments add up to much more than what the available data suggest.

Other government expenditures

The other economic categories of government expenditures are: current expenditure on purchases of commodities and services, grants, pensions, expenditure on gross capital formation, capital transfers, investment in shares of government and other concerns, etc. These categories account for a fairly large proportion of total government expenditures in India. Take, for example, current expenditure on purchases of commodities and services. Available data suggest that this category alone accounts for about one-fourth of total government expenditures in India.

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[1] Government of Rajasthan, Directorate of Economics and Statistics: Economic Classification of Budget 1975-76 to 1977-78 (Jaipur, 1978), p. 24.

DISTRIBUTIONAL IMPACT OF GOVERNMENT EXPENDITURES

One way of analysing the distributional impact of government expenditures is to estimate the benefits from the various government expenditures and to distribute them among the poor and the non-poor. But how to estimate the benefits from various government expenditures? And how to distribute the benefits from government expenditures among the poor and the non-poor? These are important, but difficult, public policy questions. The difficulty can be illustrated by considering the expenditures on, say, defence services. These services cost the exchequer Rs. 55,509.8 million in 1982-83. But what is the monetary value of benefits from these services? Is it equal to, less than or greater than the expenditure on them? And who benefits most from them? No meaningful answers are available to these questions. In view of this, all that one can do is to assume that the monetary value of the benefits from defence services is equal to the expenditure on these services and to allocate the benefits among the poor and the non-poor according to some formula.

A review of the literature shows that a number of formulae have been used to allocate government expenditures like those on defence services. These range from allocating such expenditures to the ten per cent wealthiest people (who have most to protect),[1] to

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[1] See Miguel M. Urrutia and Clara E. de Sandoval: "Politica Fiscal Y Distribution del Ingres en Colombia", in <u>Revista del Banco de la Republica</u> (Bogota), Volume 44 (1971), pp. 1072-87. Cited in L. De Wulf: "Fiscal Incidence Studies in Developing Countries: Survey and Critique", International Monetary Fund, Fiscal Affairs Department, DM/74/24, February 16, 1974, p. 22.

allocating them on an equal per capita basis.[1] With such a range, one can come up with widely differing estimates of the distribution of benefits from government expenditures on defence services. And considering that these expenditures account for a sizeable proportion of total government expenditures, reliance on widely differing formulae for allocating the benefits from these expenditures can give rise to considerably different estimates of the redistributional impact of government expenditures. This does not appear to be a happy situation.

A better way of dealing with the problem may be to concentrate on selected government expenditures, such as those on community and social services. One could then collect the details of the various government expenditure schemes included under the selected heads of government expenditures and identify the schemes, as also the corresponding amounts of government expenditure, which are intended to benefit the poor and the non-poor. This could be followed up by detailed evaluation of at least some of the schemes so as to get an idea of the extent to which the government expenditure schemes really benefit the intended beneficiaries. An exercise along these lines would be interesting in that it would throw

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[1]See Henry Wallich and John Adler: Public Finance in a Developing Country: El Salvador - A Case Study (Cambridge, Harvard University Press, 1951) and Henry Aaron: "Estimates of the Distributional Impact of Brazilian Taxes and Expenditures", Council for International Progress in Management (USA), July-August 1968, mimeographed.

meaningful light on the differences, and the leakages, if any, in the implementation of the various government expenditure schemes.

This is a good alternative, but, unfortunately, does not appear to be a viable one. This is so due to certain difficulties. To begin with, the required details of the various government expenditure schemes are not available. The numerous demands for grants and other documents issued by the central, state and union territory governments contain a lot of data, but they are not adequate for estimating the distributional impact of government expenditures. Consider, for example, the case of central government expenditure on medical relief. According to the data in Detailed Demands for Grants of Ministry of Health and Family Welfare for 1977-78 (issued by the Government of India in June 1977), a sum of Rs. 62,926,000 was actually spent on medical relief by the central government during 1975-76. Nearly one-half (Rs. 31,875,000) was spent on Safdarjang Hospital, New Delhi, and the balance on Willington Hospital, New Delhi (Rs. 16,980,000), Central Institute of Psychiatry, Ranchi (Rs. 3,806,000), All India Institute of Physical Medicine and Rehabilitation, Bombay (Rs. 2,633,000), Kalavati Saran Children Hospital, New Delhi (Rs. 3,250,000), T.B., leprosy and other medical institutes (Rs. 3,735,000) and hospital and dispensaries established in association with state governments (Rs. 647,000). The composition of the central government expenditure on medical relief is such that as much as 48.80 per cent was incurred on salaries, 24.05 per cent on materials and supplies, 6.63 per cent on office

expenses, 4.37 per cent on machinery and equipment, 0.64 per cent on maintenance, 0.44 per cent on motor vehicles, 0.29 per cent on wages, 0.11 per cent on travel, 0.10 per cent on grants-in-aid to canteen, 0.05 per cent on publications, 0.03 per cent on scholarships, 2.36 per cent on other charges, and 12.13 per cent on grants.

These are very useful data. But one would also like to know as to whom did the policymakers have uppermost in mind when formulating the budget proposals in respect of expenditure on medical relief? Was the expenditure on medical relief intended to help the poor or the non-poor? The available data do not provide any answer to these questions. It can be argued that one can obtain the required information by contacting the concerned government officials.

But this is not the end of the story. Suppose the concerned government officials say that the expenditure in question was intended to help the poor. This can be followed by an attempt designed to get an idea of the extent to which the poor actually benefited from government expenditure on medical relief. But there lies the rub: How to estimate the value of benefits from government expenditure on medical relief and how to determine the share of the poor in such value? This is a complicated question. It becomes much more complicated if one realises that while there appears to have been some improvement in the accessibility of the poor to medical facilities, it does not appear to have been reflected in reduction in the incidence of poverty.

This does not mean that we are suggesting a case for a cut in expenditure on medical relief. Far from it. All that we are trying to do is to indicate the nature of difficulties one faces when using the benefit approach for estimating the distributional impact of government expenditures.

The other way of analysing the redistributional impact of government expenditures is to make use of what is known as the income approach. What is different about this approach is that it assumes that every rupee of government expenditure generates income, regardless of the purpose for which it is incurred. What this means is that for estimating the distributional impact of government expenditures, all that one has to do is to find out who receives the incomes generated by government expenditures. Thus, if A is hired to work as a doctor in a government hospital, it will be taken that it is A who gains from what the government spends by way of his salary, allowances, etc.

But one may say that the income approach is not the best way of estimating the distributional impact of government expenditures. It may be argued that the expenditure which a government hospital incurs on a doctor by way of salary allowances, etc. should be allocated to those who benefit from the services rendered by the doctor, and not to the doctor.

There is a merit in this argument. But what about the expenditure by way of salary, allowances, etc. to those who collect taxes? According to a study financed by the Planning Commission, those who collect taxes render services which have the effect of augmenting the incomes of certain people.[1] The study has come up with all kinds of formulae for allocating the benefits from expenditure in collection of different central and state taxes. Here is an example: 50 per cent of the expenditure on account of collection of estate duty and wealth tax has been allocated according to the ownership of land by households, and the remaining 50 per cent according to the ownership of pucca houses. Does this make sense?

Similarly, how would one allocate government expenditure on education? One may argue that government expenditure on education benefits students and in turn the households to which the students belong. Good. But should one make any distinction between the utility derived by different households from government expenditure on education? Put differently, should one be concerned with the relevance or otherwise of education to the needs of different people? If not, why not? Should one make no adjustment at all for differences in the quality of education received as one moves from one place to another? That is, can one simply assume that the benefit

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[1]S.P. Ahuja: Distribution of Benefits from Government Expenditure: A Case Study in Selected Districts (New Delhi, Institute of Economic and Market Research, 1978). For a review of this study, see Anand P. Gupta: "Who Benefits from the Planning Commission?" in Economic and Politcal Weekly (Bombay), March 24-31, 1979, pp. 623-24.

received from government expenditure on education by a primary class student in a mud-walled, single-teacher school in a remote rural village is the same as in the case of a student attending an urban primary school in a pucca building with playground and other facilities?

Further, how would one deal with leakages in government expenditures? There is no dearth of leakages in government expenditure in India. One sees them in different forms: One sees them in the form of sinecures in government; one sees them in the form of overinvoicing of expenditure; and so on. No data are available on leakages in government expenditure, but available evidence clearly suggests that the amount involved is significant and that it is growing at a rate much faster than the rate of growth in government expenditures. Indeed, leakages are so rampant that by the time the pipeline reaches the intended beneficiaries it almost dries up in an increasingly large number of cases.

The question which arises here is: Would one like to use the benefit approach or the income approach for estimating the distributional impact of leakages in government expenditures? To be specific, let us take the case of government expenditure leakages in the implementation of a rural drinking water supply scheme in Rajasthan. According to an estimate, the leakages add up to about Rs. 50 million: The private contractors who were engaged for installing handpumps were awarded rates which were over 150 per

cent higher than the prevailing market rates.[1] How would one deal with these leakages. Would one like to allocate them to the intended beneficiaries of the rural drinking water supply scheme, or to the private contractors (and some government officials and others)?

One can go on raising such questions. The point being made is that it is not easy to come up with meaningful estimates of the distributional impact of government expenditures. At the same time, considering the size of government expenditures in India, attempts will have to be made to come up with such estimates.

We have made two such attempts. The first deals with central government expenditures and relates to 1973-74.[2] Its finding is that the non-poor gain much more from government expenditures than the poor do - the share of the non-poor works out to over five-sixths as against less than one-sixth of the poor. The study also compares the gain of the poor from central government expenditures with the central taxes they pay and comes up with the finding that for every rupee which the poor pay as tax, they receive only about 80 paise in return.

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[1] "Rajasthan: Scandals in the Sand", in India Today (New Delhi), April 15, 1983, pp. 72-76.

[2] Anand P. Gupta: "Who Benefits from Central Government Expenditures?" in Economic and Political Weekly (Bombay), Annual Number 1977, pp. 267-86.

The second study, which relates to 1975-76, deals with the expenditures of the central government as also with those of the different state and union territory governments.[1] The findings of this study are as follows: (a) While the poor do gain from government expenditures, their share works out to only about one-third of that of the non-poor; (b) it is the non-poor living in relatively better-off states who gain more from the food, export promotion, interest and investment subsidies given by the central government - the non-poor in Maharashtra alone gain more from these subsidies than all the poor in the country taken together do; and (c) the fiscal operations of the central, state and union territory governments have worked in the direction of making the poor poorer in terms of private consumption expenditure.

A question regarding these findings was raised in the Parliament.[2] In the answer given by the Minister of Finance, it has been stated that the assumptions made and the methodologies used in the study are not acceptable to the government and that the government would like to go by the findings of its own study.

With the Minister of Finance having said this, one hoped the government would soon undertake a study to estimate

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[1]Anand P. Gupta: Who Benefits from Government Expenditures in India? (Bombay, Centre for Monitoring Indian Economy, 1980).

[2]Lok Sabha unstarred question no. 5320 answered on March 27, 1981.

the distributional impact of government expenditures in India. Over two years have already passed, but nothing of this sort has been done. This is unfortunate.

VI. THE FISCAL POLICY THAT CAN HELP THE POOR

The message of the foregoing discussion is simply this: that growth of government in India, measured in terms of taxes and government expenditures, is not equitably reaching the poor.

This calls for reforms on the front of fiscal policy. In order that fiscal policy can be of help in dealing with the problem of poverty, it must be such that (a) it induces higher levels of growth, (b) it creates conditions such that the poor are able to significantly contribute to growth, and (c) it ensures that growth equitably reaches the poor. The question which now arises is: What kind of reforms in fiscal policy are required so that it can be of help in dealing with the problem of poverty in India? The purpose of this section is to make an attempt to answer this question.

NOMINAL TAX RATES

One can identify four areas in which fiscal reforms are required. The first relates to nominal tax rates. As things stand today, the nominal tax rates in India are generally on the high side. Take, for example, the tax rates applicable to

corporate incomes. In the generality of cases, the rate of tax on corporate income (including surcharge) currently leviable under the Income Tax Act, 1961 is 57.75 per cent (55 per cent plus 5 per cent thereof). In some cases, it is even higher. In addition, under the provisions of the Companies (Profits) Surtax Act, 1964 a special tax called surtax is leviable on companies showing high degree of profitability. Surtax is levied in two slabs. The rate of surtax applicable to the first slab is 25 per cent; that applicable to the second slab is 40 per cent.

This is one side of the picture. The other side is entirely different. It is full of provisions which, as indicated earlier in this study, enable companies to generate handsome tax savings. But what is important to note is that the tax rates which are used to compute tax liability continue to be on the high side. What happens is that these provisions are taken into account for the purpose of determining the taxable income. But once the taxable income is determined, tax liability is computed by using the applicable tax rates. And these rates are certainly on the high side.

What kind of signals do such rates give? Are they good for growth? We have carefully examined these questions. Our finding is that some of the signals are such that they cannot be regarded as good for the growth of the Indian economy.

In our view, the system of corporate income taxation can make a much better contribution to the growth of the Indian

economy. But for this to happen, certain things will be necessary. To begin with, we believe there is a strong case for the withdrawal of the surcharge on income tax payable by companies. One does not know what purpose this serves, except that it helps in raising some fiscal resources. But if that is the purpose, let the government straightaway raise the rates of income tax payable by companies. We see no justification in resorting to gimmicks such as the surcharge on corporation income tax. Withdrawal of the surcharge on corporation income tax will be of help in improving the economic environment which in turn can be expected to induce faster growth.

There is also a case for a good look at the surtax. Not much money is being collected on account of this tax: According to the data compiled by the Public Accounts Committee, the actual collections on account of this tax amounted to Rs. 273.9 million in 1976-77, Rs. 557.9 million in 1977-78, Rs. 478.4 million in 1978-79, Rs. 322.6 million in 1979-80, and only Rs. 215.4 million in 1980-81.[1] Put differently, the share of surtax in total tax collections has declined from 0.42 per cent in 1977-78 to 0.31 per cent in 1978-79, 0.18 per cent in 1979-80, and to 0.11 per cent in 1980-81. Nobody seems to know why this has been happening. Even the Ministry of Finance doesn't know why the collections from surtax have been declining:[2]

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[1] 1980-81 is the latest year for which data on actual collections on account of surtax are available.

[2] See Lok Sabha Secretariat: One Hundred and Forty-third Report, Public Accounts Committee (1982-83) (New Delhi, Mimeographed, pp. 14-17.

It appears that not many companies pay surtax. Although the tax has been in force for nearly 18 years, it has not served any visibly useful purpose.

Finally, we believe that a reduction in corporation tax rates is necessary. As we noted earlier, the present rates are on the high side. Lower rates of tax on corporate income will give signals which can be expected to have beneficial effects not only on the climate for investment but also on that for output and employment. Some people may argue that a reduction in corporation tax rates would encourage companies to distribute larger dividends. We do not see any thing wrong with an outcome such as this. Indeed, we believe the economy would be healthier if companies distribute not less but more of their incomes and if the additional money paid in dividends is mobilised through a dynamic capital market.

FISCAL BIAS IN FAVOUR OF CAPITAL

The second area in which reform is required relates to fiscal provisions which have an influence on the employment of labour in the modern factory sector in India. The link between the growth of this sector and employment appears to be quite weak. The Planning Commission has described this link as follows: "A look at the distribution of workers in India in seven decennial censuses 1911-1971 shows up the historically unique fact that in spite of an impressive development of large-scale manufacturing and infra-structure sectors, the share of agriculture in the work force has

not diminished at all. It was 72 per cent in 1911, 73 per cent in 1961 and nearly 74 per cent in 1971 .... In almost all countries economic development is associated with a significant decrease in this share .... In India, however, a fairly rapid growth in the non-agricultural sectors during the last twentyfive years of planned development has not made any noticeable impact on the industrial distribution of the work-force. For six decades the share of mining and manufacturing in the work-force has stuck around 9 to 10 per cent and that of the tertiary sectors around 16 to 18 per cent. The inference is clear: employment growth in these sectors has been insufficient to absorb an increasing proportion of the labour force. Investment and output have grown at a high rate but the production-mix and the technology-mix have been so capital-intensive that employment did not grow _pari passu_."[1]

In our opinion, spread of industrialisation can be of much help on the front of employment if the present bias of fiscal policy in favour of capital is removed. There are a number of fiscal provisions in India which have a _prima facie_ bias in favour of capital and which, there is reason to believe, encourage the use of capital in capital-intensive ways. Take, for instance, the provision relating to investment allowance. The provision is so designed that the amount of tax benefit varies directly with the amount of

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[1]Government of India, Planning Commission: _Draft Sixth Five Year Plan 1978-83 Revised_ (New Delhi, 1979), p. 132.

capital invested in new plant and machinery. The higher the amount of capital so invested, the larger the amount of tax benefit. Thus, if a company instals a new machine costing, say, Rs. 1 million, it will be entitled to claim an investment allowance of Rs. 250,000 (Rs. 350,000 in the case of a machine installed for the manufacture or production of an indigenously developed article or thing, or for pollution control, or for protection of environment) and a tax benefit of Rs. 144,375.[1] This, in a way, means that the scheme of investment allowance has the effect of reducing the price of the machine by 14.44 per cent (20.21 per cent in the case of a machine installed for the manufacture or production of an indigenously developed article or thing, or for pollution control, or for protection of environment).

A/number of companies avail of the benefit available / large under the scheme of investment allowance. Available data show that the machines which the companies instal are generally of a labour-displacing type. Available evidence also suggests that trade unions do not generally object to the installation of such machines. All that they insist on is that the workers (including those who are retrenched) get a share in the benefits resulting from the installation of labour-displacing machines. The public financial institutions,

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[1] Arrived at by using the rate of corporation tax (including surcharge) currently applicable to the generality of cases, viz. 57.75 per cent (55 + 5 per cent thereof).

on their part, facilitate the installation of such machines by providing the necessary finance.

The scheme of investment allowance was examined recently by the Dandekar Committee. According to the Committee, the scheme has a *prima facie* bias in favour of capital-intensive technology. The Committee, therefore, recommended that the scheme be discontinued.[1]

Incidentally, the Dandekar Committee had also examined the provision relating to tax holiday (section 80 J). The Committee found that although tax holiday also induces capital intensity, the capital bias resulting from it is not as acute as that from investment allowance. In order that the bias of the tax holiday scheme in favour of capital intensity is removed, the Committee recommended that the benefit of the scheme be made available in terms of the profits of a new industrial undertaking without any reference to the size of the capital employed. The government has already implemented this recommendation of the Committee.

The point to note is that while the government has accepted the Dandekar Committee's recommendation in respect of tax holiday on the ground that "the fiscal system should not lead to a bias in favour of capital-intensive techniques", it has not accepted the

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[1] Government of India, Ministry of Finance, Department of Revenue, *op. cit.*, pp. 30-33.

Committee's recommendation in respect of investment allowance. Considering the fact that the capital bias resulting from investment allowance is more acute than that from tax holiday, one wonders why this is so.

If for one reason or another the government is not able to withdraw the scheme of investment allowance, it should at least do away with the requirement that the investment allowance reserve (which the assessees claiming investment allowance are required to create) has to be used for acquiring new plant or machinery within a period of ten years. The case for this requirement does not appear to be strong. Discussions with knowledgeable people suggest that this requirement may unnecessarily force industrial enterprises to go in for plant and machinery which they may not need at a point of time. An outcome such as this can not be regarded as good, especially when it is being argued that the rise in incremental capital-output ratio in India has nullified the output increase that otherwise would have come from the increase in the share of investment to income and that the key to future industrial growth in the country lies in decreasing the capital-output ratio.[1]

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[1]See C. Rangarajan: "Some Reflections on Industrial Growth", RBI Endowment Lecture, Indian Institute of Management, Ahmedabad, December 1, 1981.

FISCAL MEASURES TO PROMOTE EMPLOYMENT

The third area in which reform is required relates to measures taken to promote employment. The Government of India and the various state and union territory governments have taken a number of measures for promoting employment. A complete inventory of all the measures taken for promoting employment is not available, but it would be safe to say that it is through the fiscal system that many of such measures have been implemented. For instance, the system of central excise taxation seeks to promote employment through wide-ranging exemptions and concessions in excise duties to products of labour-intensive technologies and small scale industries. No duty is leviable on a number of commodities if no power is used in their manufacture. Examples are confectionery, food products, vegetable non-essential oils, paper and paper boards, manmade fibres and yarn, cotton yarn, woollen yarn, silk yarn, jute yarn, mineral fibres and yarn, grety cotton fabrics manufactured on handloom, khadi cloth, footwear, steel furniture, bolts, nuts, screws, metal containers, safes and strong boxes and adhesive tapes.

In addition, the excise system has provisions to give preferential excise treatment to relatively labour-intensive sectors within an industry. The match industry is a case in point.

Similarly, there are provisions to give excise relief to small manufactuers of a large number of commodities. The benefit on account of these provisions is so great that most of the small scale manufacturing units end up paying little or no excise duty at all.

It is good to see that the fiscal mechanism has been used for promoting employment. But one is not sure if all that is required has been done. One is also not sure if all that has been done has been along the right lines. There is a strong case for a good look at the entire system of fiscal support of labour-intensive technologies. Some of the issues which merit consideration are: How does one identify labour-intensive technologies for fiscal support? How does one determine the scale and period of fiscal support? How does one estimate the fiscal cost of supporting a labour-intensive technology? How does one monitor the impact of various fiscal measures taken to promote employment and judge their appropriateness or otherwise?

REFORM IN GOVERNMENT EXPENDITURES

Finally, there is a strong case for reform in government expenditures. Indeed, the case for government expenditure reform is much stronger than the case for tax reform.

The reform will have to be along two lines. First, much more money than allocated so far will have to be allocated for

programmes designed to help the poor in augmenting their incomes. Integrated Rural Development Programme and National Rural Employment Programme are good examples of such programmes.[1] When presenting the central, state and union territory budgets, let the finance ministers indicate clearly the total amounts allocated for programmes intended to help the poor. Taxes raised from the poor must be earmarked for such programmes. A part (say, one-third) of the taxes raised from the non-poor should also be so earmarked.

Second, there will have to be a war on waste in government expenditures. A general impression which has gained ground in public mind is that a good part of government expenditure is of wasteful nature and serves no public interest. Indeed, there is a widespread feeling of disappointment with the way government money is spent. It is, therefore, necessary to take immediate action for an examination of the system of government expenditures in its entirety with a view to systematically identifying the various leakages in it. Once the various leakages have been identified, determined efforts will have to be made to plug them.

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[1] For a description of these programmes, see Government of India, Planning Commission: Report of the Expert Group on Programmes for Alleviation of Poverty (New Delhi, 1982), pp. 9-30.