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THE ROLE OF TAXATION IN PLANNED ECONOMY

~~Prof [illegible]~~

~~[illegible] Budget~~ I

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Acts & Speeches

Classical purpose of taxation

To Cover Governmental expenditure

Govt

[redacted] Army and Wars

Police

Civil service

In welfare state and planned economy additional purpose
Broadly economic development plus social justice

/ Economic Development.

Increase in sum total of goods and services

Production precedes distribution

Increase size of cake

Khrushchev (Time, May 4, 1962) "If Communism is proclaimed where there is, say, one pair of pants per ten persons, and these pants are divided equally into ten parts, we shall all be going without pants. We reject such pants-less Communism."

K: Ball pen
[illegible] Gagarin

<u>How?</u>

(a) By providing resources for infra structure
namely: irrigation, transport, communication, power and fuel,
technical and general education.

Role of State that of traffic policeman not motorist : referee, not pugilist.

(b) By providing fiscal incentives ~~xx~~ to save and invest
namely : capital formation
profit motive as incentive
profit a yardstick of efficiency
no economic progress without it.

Khrushchev at 22nd Congress of C.P.S.U. 1961 warned against reckless haste in leaping into communist practices in the field of distribution and wage policies. He emphasised that wages must remain the principal stimulus to work for a long time to come and that the rewards of labour should be distributed according to the work done.

London Times (on Communist regime in Yugoslavia in April 1961)

"Profitability, productivity and competition are no longer ideas on paper but are beginning to affect and change individuals as much as they are affecting the enterprise they work in. It is this, the recognition of economic incentive and the free formation of prices through competition and market conditions, which distinguishes Yugoslav Communism sharply from that of the Soviet bloc."

CED: "Taxes must be high enough to cover the expenses of Government over the years, but not so high as to repress growth, or to inhibit risk taking and individual initiative; high enough to create a surplus in prosperous times, that provides funds for private investment through retirement of government debt, and helps restrain inflation, but not so high as to prevent the attainment of high employment."

In under-developed countries need for incentives all the greater

Parkinson's The Law and the Profits (Page 95)

"With peacetime taxation amounting to over 10 per cent of the national income, capital will begin to migrate. If its flight is prevented, whether by circumstances or by legislation, taxes can rise to 20 per cent but against a stiffening opposition which takes the form of tax avoidance and evasion carried to the utmost lengths of determination and skill. Above 20 per cent each tax increase will produce proportionately less. Above 25 per cent there is serious inflation, reducing the value of the revenue collected. Above 30 per cent the decline in national influence, observable long before to the expert, becomes obvious to the world at large. At 35 per cent there is a visible decline in freedom and stability. At 36 per cent there is disaster, complete and final although not always immediate. Taxation beyond that point, feasible and perhaps necessary in time of war, is lethal in time of peace. Of the taxation precipice, 36 per cent (for most countries) represents the brink."

~~CED [illegible]~~

But capital not only element in productivity

other three equally important - Land

Labour

Enterprise

Human factors often overlooked

Colin Clark (Growthmanship) Better knowledge

Organisation

skill

effort

education and ~~enterprise~~ enterprise.

2. Social Justice

How taxation can influence?

(a) Stable currency, so people may enjoy fruits of their labour and enterprise
Inflation - anti-social and anti-socialist
High cost structure which results bad for export.

(b) Equal pay for equal work
Involves just differentials
Accepted in U.S.S.R. since 1932
Equality declared "petty bourgeois deviation"

(c) Satisfaction of psychological factors
Justice should <u>appear</u> to be done
The have-not's point of view

Right to work and employment; needs of consumption

Apart from justice, two additional arguments from development point of view:

(i) nutrition etc. essential for efficiency and productivity
Thus <u>some</u> consumption must preceed production.

(ii) Purchasing power spread wide is stimulant to employment and growth.
Creates market.

3. Balancing of considerations of growth and social justice leads to establishment [redacted] of priorities.

(all except Communists)

At recent seminar in Delhi, happy to find agreement on proposition that satisfaction of basic needs of food, clothing and shelter along with ~~with~~ some medical relief and education, accepted as first priority of planning. S.P. Manifesto

Working Group to explore implications.

Galbraith (On the theory of Development Planning - Economic Development in Perspective pp.26-34)

"....nothing is so important as abundant and efficiently produced food, clothing, shelter, for these are the most and universal of requirements."

Galbraith (The Affluent Society : pp)

"To give people income and then remove it by taxation, inflation or appeals to thrift is an inefficient and self-limiting procedure....In poor and ill-governed societies, private goods mean comfort and life itself. Food, clothing and shelter, all technically subject to private purchase and sale, have an urgency greater than any public service with the possible exception of the provision of law and order. The burden of proof is on any step that diverts resources from the satisfaction of these simple biological requirements to the almost invariably spendthrift services of the State."

Great Leap Forward: Mao View.

China - National People's Congress in April 1962 laid down their new policy for "all round balance" between branches of economy in "the order of agriculture, light industry and heavy industry".

Swatantra Party [illegible]

This involves employment opportunities for all able-bodied adults.

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II

Define scope of enquiry : to what extent do taxation in India and current Budget conform to these objectives of a planned ecomomy?

(Exclude wider discussion of Planning)

1. Economic development

(a) Infra structure grossly neglected

Irrigation

Roads - neglect of roads

dog in the manger policy of State Railway Monopoly.

despite a crying need to open up country side,

high revenue yield of road transport and

high employment potential.

Despite these roads starved and 20% of Second Plan outlay

spent on Railways and Third Plan just as bad.

During III Plan, exp. on roads Rs 500 crores

Tax on motor transport Rs 900 crores.

Tax on ton mile exceeds entire cost of ~~freight~~ per ton mile on Railways.

Tax - Multiplicity - 30% of initial cost of bus

32% of revenue of diesel bus

29% " petrol vehicle

Thus bus fares forced up 30-50% higher than III class rail

Power - O.V. Alegeson in Parliament (21.5.1962)

Admitted ½ mill. Kw. by 1965-66 shortage

Fuel - P.M. at F.I.C.C.I Annual Meeting accepted criticism of Government Policy of coal, power, and transport as "largely justified."

Education - neglect of education

total expenditure on primary and secondary education during Second Plan period Rs.1,350 million

while three steel plants cost Rs.5,260 million - four times as much.

Expenditure on primary and secondary education in India was only 0.96 % of the Budget outlay at the Centre and in the States. Corresponding figure from many other countries varies from 7 to 12 times as much as the Indian figure.

(b) Incentives to save and invest

On the contrary - tax pattern provides disincentives
Tax burden at top level can exceed 100% of income.

At the level of income above Rs.26,660, tax burden higher in India than in most advanced countries like U.S.A., U.K., West Germany, France, Canada and Japan.

Man with an annual income of Rs.106,000 taxed at the rate of 53.1%. Higher than any other country with the sole exception of Norway. Comparable rates of taxation in other countries are

Norway	62.8 %
U.K.	46.2 %
Japan	36.8 %
West Germany	35.5 %
Canada	27.1 %
France	25.9 %
U.S.A..	23.1 %

Mr. Richard Perkins (Chairman of the Executive Committee of the First National City Bank of New York.) :

"We operate in 30 countries and I find the tax rate here in India is the highest".

Cf Gross profits with UK – 1955-57

This year's Budget aggravates situation by raising tax on corporate profits from 45 to 50% and also tax on personal incomes.

~~NCAER~~

Planning Commission ~~N.P.C.~~, had already observed in Third Plan document that limits of direct taxation had been reached and no increase possible.

But Finance Minister acting against this caution.

This Budget thus one more of a bad bunch. cf [illegible]

Retarding economic development. [illegible]

Saddest part of story, proceeds of taxation going predominantly towards unproductive, non-developmental expenditure. Estimates Committee of Parliament pointed out that large part of the additional taxation levied during Second Plan period diverted to non-plan expenditure.

Cost of Administrative Services gone up in the last decade by Rs.370 million.

Parasitic expenditure - Parkinson's Law exceeded.

Result -

National Council of Applied Economic Research (Study of 1961)

> "The rate of growth of paid-up capital of operating registered companies has fallen from 10.4% in 1951-52 to 3.6% in 1959-60 ......Nor is it correct to say that the rate of profits in the industrial sector has gone up since 1951. The index of profits after tax as a percentage of net worth for all industries worked out by the Reserve Bank of India (on the basis of a sample of companies) has actually shown a declining trend. The index (with 100 in 1950) stood at 124.7 in 1951 and 84.1 in 1957."

The second trend to emerge is that the rate of saving is stagnating:

> "Over the second Plan period the rate of savings in the economy has not risen at all, but has stagnated around 8% of the national income."

Drawing certain conclusions, the Report says:

> "It has been often suggested that in India higher taxation is an important method of financing public investments. Whatever may be the theoretical merits of this proposition, in practice it is found that current expenditure under the Plans as well as outside them is rising so fast that even substantial increases in tax revenues are almost wholly absorbed by the rise in such current expenditure; with the result by far the greater part of public investment has to be financed through a draft on private savings and foreign aid..........In this situation the need to promote a higher rate of private saving deserves the Government's closest attention."

The Report comes to the conclusion that

"individuals must be allowed, even encouraged to accummulate sufficient amounts of wealth.......We recommend that the pace of progression of super-tax be reduced so that the highest marginal rate will become operative at a higher level than at present."

1) Further Steepening

Present Budget - 2) All additional taxation to be eaten up by revenue deficit made up of civil and military non-developmental expenditure.

Thus net income in pocket of people declines.

Result - both consumption and saving decline.

Saving more than consumption since no margin ~~of cut~~ in consumption of big majority.

No category favoured of Capital Loans - Quote Palkhivala

Hindustan Times (24.4.1962) "If this Budget had been merely anti-capitalist few tears would be shed. But since it is anti-capital as well, there is cause for national concern... .....Direct taxes are clearly taxes on employment and the opportunities that may be available to the people for making a livelihood."

~~Necessity~~

c.f. What's happening abroad?

Last Budget in Britain gave tax relief to middle class .

U.S. Kennedy proposes slashes amounting to 25% overall in taxes on individual income ~~taxes~~ plus reduction in corporate taxation from 52 to 45% (but U.S. News and World Report says 49%) - (Kiplinger Washington Letter)

Maximum individual IT rate to come down from 91% to 65%.

Kennedy (Time - May 11, 1962 - page 9) : "We want prosperity, and in the free enterprise system there can be no prosperity without profit. We want a growing economy, and there can be no growth without the investment that is inspired and financed by profit."

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2. Social Justice.

(a) Stable currency

On the contrary - reckless inflation.

Value of Rupee falling since 1955-56 at rate of 6.5 % p.a. over past 6 years

Total - 39%

Highest in world for corresponding years.

In terms of pre-war rupee equal to 20.6 np.

Family of head clerk drawing Rs.300 before the War equals the salary of a Deputy Secretary at Centre drawing Rs.1440/- today (Shenoy).

Caused by

(i) Deficit finance

(ii) Excise duties

(iii) Investment pattern

0.5

0.3

0.4

Steel - Investment Rs 1000 crores. Loss 60 crores (G.D. Birla Commerce Souvenir Bom)

Pity Balkrishna Wasnik's resolution rejected in Lok Sabha

Undeterred by experience.

Latest announcement: Government proposes to set up piggeries in State Sector (Times of India - 23/5/1962)

Not surprising that as a result in the list of developing countries in Asia prepared by U.N. India appeared 28th, near bottom of list (Hindustan Times - 5/5/1962

Obvious great deal of our money placed on the wrong horses.

High cost structure ~~which~~ results inhibits export which ~~is~~ vitally needed.

Latest decision re 2% cess on output of all major industries to subsidise dumping abroad will make things ~~wose~~ worse.

Exports only

1. If prices competitive in world market
2. if imports allowed.

You cannot have one without the other.

Bankruptcy staring — Biggest [illegible] — [illegible]

E. Black "Everytime he opens his mouth"

"Cheaper to stop him travelling abroad than all others put together."

(b) Reasonable differentials.

Too much progression

This discriminatory and unequal - based on envy.

Gives unequal reward for the same work.

e.g. two doctors and lawyers doing the same job retaining different incomes because total incomes unequal.

Progression should be moderate to off-set regressive nature of indirect taxation.

~~No carrying forward of Capital Losses — Don't [illegible]~~

3. Priority for basic needs

Let us examine:

(a) Food - Agriculture neglected

70 % people live on land, but more than half outlay on development spent on industrial enterprises in State sector.

Average rise in national income during past decade (based on 1949-50 level) has been 1.8. Agriculture rise 1.4.

S.K.P.'s optimism unjustified -

1956-57 Production of food grains 69 million

1961-62 10 million tons more -79 " app. 14.5%

Total increase in last five years ~~less than~~ 15%

Third Plan target - 100 million tons by 1965-66 , i.e. 26 % increase in next 4 years.

Quite unlikely.

Even poorest peasants taxed by land revenue

No exemption limit

Hence abolition of land revenue demanded, with replacement by agricultural IT if necessary.

Need for capital investment in land.

(b) Cloth

Ban on automatic looms and modernisation.

Killing excise.

With latest impost, textile industry will contribute Rs.90 crores p.a. out of the total excise revenue of country of Rs.500 crores, i.e. 18% by cloth alone.

Root of evil - PM!s thinking

Colin Clark (<u>Growthmanship</u> : Page 28 - footnote)

~~"Not only with capital investment as such, but capital investment in its more conspicuous and symbolic forms, such as steel mills~~. In an unusually foolish statement Mr. Nehru (quoted in Freedom First, Bombay, October 1960) said "A number of textile mills is not industrialisation. It is playing with it.......Industrialisation is a thing that produces the machines. It is a thing that produces steel". It is a pity that nobody has been able to explain to Mr. Nehru that even the most advanced industrial countries still have to import many of their capital goods from each other - and that many of the Indian steel mills, so painfully acquired, will be obsolete in a few years' time."

(c) Building Materials

Excise on cement despite admitted shortfall in production.

S.T.C.'s parasitic role.

Thus clear pattern of taxation inimical to satisfaction of basic needs. Present Budget aggravates burden on poor.

Of additional taxation in 1961-62, 74% of tatal came from taxes on commodities; except for 12% on luxury goods - burden on necessities of life. This year, of additional revenue collection of Rs.72 crores, about Rs.45 crores come from commodity tax (62%) while only Rs.27 crores (38%) come from direct taxation. (~~Shenoy~~ - Times of India, May 2, 1962.)

This inevitable since well-to-do already taxed beyond limit. Higher taxation therefore means bigger burden on poor.

Shenoy : "The choice is between less taxation and more social justice on the one hand and on the other more taxation and less social justice. We cannot have more taxation and more social justice at the same time. (Times of India, May 2, 1962.)

Conclusions.

1. Abolition of land revenue cf Andhra [illegible]

2.

2. Drastic reduction in excise on necessities, raw materials and intermediates.

3. Reduction in corporate taxation and drastic reduction in direct taxation on income.

4. Strict abstention from deficit finance and other inflationary measures: cutting your coat according to your cloth.

5. All this made possible by drastic reduction in civil expenditure, and proliferating bureaucracy.

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