THE UNION BUDGET, 1972-73

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"People must come to accept private enterprise not as a necessary evil, but as an affirmative good."

—Eugene Black

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By

N. A. PALKHIVALA*

Last year's Budget was criticised on all hands as a crippling Budget. If this year's Budget has evoked no such widespread comment, it only shows the extent to which the public mind can be conditioned to lose perspective and to accept what it has no hope of changing. There is not a single relief in this year's Budget as compared to last year's. On the contrary, new levies were imposed in the mini Budgets of October and December 1971, which would aggregate to Rs. 500 crores in a full year, and which are all continued. In addition, this year's Budget proposes new taxes which will amount to Rs. 183 crores, and contains a dark hint of additional burden on individuals which may be imposed later in the form of clubbing together of the incomes of husband and wife.

The human mind is more malleable than gold; and can be easily conditioned to accept injustice and unfairness through exposure to such an environment. In India for centuries the

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people accepted the caste system with all its ugly iniquities. The Russians, with all their greatness, do not seem to have any extensive protest inside their own country against the practice of confining some of their best creative writers in lunatic asylums only because of their criticism of certain policies pursued by their government.

The value of the Budget and the relevance of the Budget proposals should be determined by reference to three questions:

(i) Does it see and seize the moment of opportunity which has come to India?

(ii) Will it achieve the short-term objectives laid down by the Planning Commission for the Fourth Plan?

(iii) Will it achieve the long-term goal of economic growth with social justice?

It is difficult to heap encomiums on the Budget in the light of these questions.

It has been said that the Finance Ministry's task has been a difficult one. We have had to spend Rs. 325 crores on refugees from Bangla Desh and propose to make commitments amounting to Rs. 200 crores for assistance to that country. We shall have spent Rs. 1,411 crores on defence during the current year and propose to spend about the same amount next year. But India can take these burdens in her stride. What the faceless men in the inflexible Finance Ministry have not appreciated is that we have now an opportunity which comes rarely to any democracy. This is the moment of absolute political stability. The ruling party has a gigantic majority in Parliament and in the State Legislatures; the whole nation is united and has a sense of euphoria following the victory; and there is a tremendous upsurge in the people's morale. In such an unprecedented year of happy auguries, the Budget could have lifted the nation's eyes to new goals of unprecedented growth; but instead it has chosen to tread the same old unimaginative path.

The burden of income-tax and wealth-tax combined, which is the highest in the world, is proposed to be continued without any abatement. It is still possible to become wealthy in India, but not by mere ability, industry or enterprise, or even by a combination of all the three. The five classes of the new rich are — tax evaders, black marketeers, bosses of co-operatives, prosperous farmers and some successful politicians.

Our Finance Ministry has stubbornly refused to learn the lesson that very high direct taxation achieves little in bringing up the standards of the poor. It is evaded by the very rich and too often catches the most deserving.

The fundamental question is — will the Budget achieve the goal of economic growth with social justice? The Finance Ministers' Speeches accompanying the Budgets invariably answer the question in the affirmative; and practical experience of the last several years invariably answers the question in the negative. This year's Budget will join several past Budgets, with their crippling levels of taxation, to constitute a supreme ironic procession, with the laughter of the God of Wealth in the background.

At the outset, it may be convenient to get one popular fallacy out of the way. Social justice is often confused with mere equality. Social justice demands that there should be adequate differentials for ability and hard work, for education and expertise, for risk-bearing and willingness to take responsibility. Elimination of such differentials is the very negation of social justice; — it is unfair to those who are denied the fruits of their industry, integrity and intellect, and it is equally unfair to the tens of millions whose hope will die within their hungry hutments, since there can be no economic growth without such differentials and there can be no alleviation of poverty without economic growth.

The vital point which is normally missed in political histrionics is that while it is possible, in a poor country like India, to have economic growth without social justice, it is impossible to have social justice without economic growth.

We live in a strange world where socialism has taken the place of the Mantras and the Shastras, the Ten Commandments and the Golden Mean. But just as a coin gets defaced and its engraving gets erased after it has been a long time in circulation, words like "socialism" get denuded of their true content after they have been in constant circulation. There is the brand of socialism which has built up the lucky countries of Europe and of the Third World. And there is also the other type of socialism which has brought down other countries like Burma, and Indonesia under Sukarno.

The four significant measures of a country's development are — an increase in the gross national product, availability of work, distribution of income, and the quality of life. The first connotes economic growth, while the last three spell social justice. You must have all the four if you want economic growth with social justice. It is true that we cannot live by the gross national product alone; but there would be no availability of work, no income to distribute, and the quality of life cannot be made less shoddy, unless and until we have a fast and sustained rise in the gross national product. The official Budget Speeches ceremoniously pay lip service to these basic propositions, while the Budget proposals continue to be cast in the mould which represents the very negation of these incontrovertible truths.

Our savage rates of personal income-tax and wealth-tax aim at attaining mere equality without learning from past experience that they inhibit economic growth, encourage large-scale evasion, and thus make it impossible for the Government to undertake any sizeable measures of social justice. Our income-tax rates go up to 97.75%, and wealth-tax rates go up to 8% (plus 7% in the case of urban property): they virtually amount to annual confiscation of income and wealth. The tax structure is such that it is more profitable for a citizen at a certain level of income to evade tax on Rs. 30 than to earn Rs. 1,000 and pay the tax honestly. Our income-tax rates are too high, not only at the top slab but all along the line. In a heavily taxed socialist country like the United Kingdom, an assessee with three children and a widowed mother and paying the usual insurance premium would be taxed at the average rate of 5.5% on an income of £1,500 (Rs. 28,845). The same income, under the same conditions, in India would attract 18% income-tax.

The elimination of poverty as a social problem is a formidable objective, but it is not an insurmountable one. We have abundant natural resources and all the man-power we need. Perhaps there is no other nation which has in such ample measure all the enterprise and skills needed to create national wealth, and which takes such deliberate and endless pains to restrict and hamper its creation. W. H. Hutt published last year his book "Politically Impossible...?" and quoted a leading economist who suggested that the title of the book would embrace "all the reforms which would be really worth undertaking". If wise changes are ruled out by politics, it is a terrible indictment of the functioning of the democratic process.

Mr. Michael Lipton and Professor P. T. Bauer have observed that the caste system and the "contemplative, non-experimental" attitude of our people are substantially responsible for our economic backwardness. Greater responsibility for our present industrial stagnation must be ascribed to the crushing burden of direct taxation.

The Wanchoo Committee which consisted of eminent men who were nominated by the Government and by no "vested interests" has devoted months of hard labour to understanding the problem of tax evasion and finding fair solutions. The Committee has recommended that the maximum marginal rate of income-tax should be brought down to 75% along with reductions at lower slabs. Within hours of the Committee's Report being made public, there have been ill-conceived attacks on the Report from certain quarters. In every country there are always some politicians whose devotional fervour, real or ersatz, for confiscatory taxation on others as an instrument of equality, wholly drenches their sense of true social justice and their understanding of the economics of growth. It is not from the distorted view-point of such politicians that the Government should consider the Wanchoo Committee's Report. Some people may consider tax cuts reactionary. But the real reactionaries are those who will not see and seize the opportunity of achieving our cherished goal by realistic policies.

The Planning Commission, in its Mid-Term Appraisal, has pointed out that one of the main causes of the fall in development is the paucity of savings and investment. The rate of national savings has decreased from 11.1% in 1965-66 to 8.3% in 1970-71, whereas savings amounting to 18 to 20% of the national income would be necessary for self-generating growth. The average annual increase in gross investments in the first two years of the Fourth Plan may be no more than 4.8%, as against the target of 9.8% implied in the Plan. Could there be any doubt that increasing taxation is the prime cause of this deplorable state of affairs?

The corporate sector has been severely hit by the increased levies during the last twelve months. With the abolition of the relief available to priority industries and the imposition of 5% surcharge, the effective rate of tax on priority industries, which was 50.6% in 1970, will go up to 57.75%. Further, development rebate is to be abolished in 1974. In a matter of thirteen years, the effective rate of corporation tax which was 40% in 1960-61 (after taking into account development rebate) will be nearly 58% (after the abolition of development rebate) — an increase of 45%. It is clear that the idea behind the Budget is to restrict the growth of the private sector and to make it impossible for it to have adequate savings, so that it is compelled to go to government controlled institutions for finance, sometimes even for the purpose of ordinary maintenance and bare replacement.

Corporate savings, which were 8.9% ten years ago, have dropped to the abysmally low level of 5¼%, although the amount distributed as dividends has remained almost constant. It is impossible to reconcile the basic philosophy underlying the Budget with the Planning Commission's observation in its Mid-Term Appraisal, "The expansion of the corporate sector and enabling it to achieve reasonably good profitability must, therefore, form another major plank of a well-conceived savings strategy".

In the Mid-Term Appraisal, the Planning Commission has further pointed out that industrial growth has "widespread ramifications" including the supply of larger financial resources for the Government, expansion of employment opportunities, maintenance of price stability, facilitating import substitution, encouraging exports and ensuring "an adequate availability of basic consumption needs". The Planning Commission wants the industrial sector to grow at the rate of 10.1% during the remaining period of the Fourth Plan. With proper fiscal incentives and other changes in our policy, we can easily have a 12% growth in the corporate sector, which would generate Rs. 930 crores additional annual revenues for the Union Government alone, apart from massive additions to the revenues of the States.

The latest Budget just introduced in the United Kingdom constitutes an interesting exercise in the art of generating growth through tax cuts. Prior to the introduction of the Budget, the Trade Union Congress, the apex body of the working class in England, itself recommended a cut of £ 1,500 million (Rs. 2,885 crores). The National Institute of Economic and Social Research, which is a prestigious expert body, recommended a cut of £ 2,500 million (Rs. 4,808 crores). The Chancellor of the Exchequer has actually effected a cut of £ 1,200 million (Rs. 2,308 crores). This huge cut is in an amount which is more than half of the entire revenue budget of our Union Government. With this tax cut the U.K. expects to double its rate of growth and reduce substantially the number of the unemployed. The policy now adopted in the U.K. is the modern fiscal policy pursued by the most progressive countries, which makes revenues grow, while actually decreasing income-tax rates, by making incomes and the gross national product grow. Although the problem of unemployment and economic stagnation is much more dangerous for a poor country like India than it is for the United Kingdom, we have chosen to go in the contrary direction and have substantially increased the fiscal burdens since the beginning of the present Parliament.

The Index of Industrial Production rose by 6.6% in 1958-69 and 6.9% in 1969-70. But the increase declined to 3.5% in 1970-71, and is likely to be less than 4% in 1971-72. This pathetic level of growth puts India at the lowest level of the developing countries of the world, — we have for company Burma, Congo, Haiti, Mali and Somalia. So long as we continue to persist in the policy of deliberately restraining the growth of the private sector by the budgets and policies which are in vogue today, an optimum rate of growth must be altogether ruled out.

We have rightly adopted a wise and humane policy towards Bangla Desh and propose to make commitments for assistance amounting to Rs. 200 crores. If a fraction of the same understanding and helpfulness could be extended to our own industries at Budget time, what a difference there would be between this picture and that!

If the Budget, instead of abolishing the priority status of industries whose development is so essential from the national standpoint, had reduced the rate of tax on them to 40%, and reduced the rate of tax on other companies to 50%, the total loss to the revenue would have been Rs. 90 crores. This shortfall could have been easily met by making a correspondingly lower provision for Central and Centrally sponsored Plan schemes, even if the Finance Minister had chosen to ignore the larger revenues which would be generated by the dramatic impetus to development. The Budget provision for such schemes is Rs. 1,787 crores, representing an increase of Rs. 332 crores over a similar provision for the closing year. The suggested reduction in corporate taxation would have given a much greater boost to the economy than the unreduced provision for the Plan outlay. Even after reduction by Rs. 90 crores the Budget provision for Plan schemes would have still been higher by Rs. 242 crores for the next year as compared to 1971-72. Further, in reality there is bound to be a heavy shortfall in the actual expenditure on Plan outlays. In other words, it is most improbable that the Union would actually spend Rs. 1,787 crores by way of Central Plan outlay, as provided for in the Budget. The figures of similar shortfalls in Central Plan outlays were about Rs. 100 crores in 1971-72, Rs. 160 crores in 1970-71 and Rs. 236 crores in 1969-70. Thus, without disturbing any other part of the Budget, a tremendous fiscal stimulus could have been given to industry by lowering the rates of corporation tax and correspondingly reducing the provision for Plan outlay.

The magnitude of the Herculean task facing India can be gauged from the fact that even if the rate of our industrial growth can be pushed up to 6% per annum, it would take us 20 years merely to double our per capita income.

Social justice demands that the unfortunate unemployed should be given jobs. The unemployed number 14 million today at a conservative estimate, and the figure is expected to go up to 37 million by 1980. Since the Budget will constrict economic growth, it will necessarily reduce job potential and availability of work and thus defeat one of the main goals of social justice.

As regards the problem of distribution of income, the tiresome truth needs to be repeated that you cannot divide more than you produce. It has been calculated that if the income of everyone earning over Rs. 25,000/- annually were to be equally distributed amongst all, it would mean only a rise of 40 paise in the annual per capita income. In trying to achieve the objective of levelling of income, our annual Budgets merely succeed in widening the gulf between the dishonest rich and the poor, and narrowing the gap between the honest rich and the poor.

If the men in power are earnestly and sincerely anxious to achieve the goal of economic growth with social justice, they cannot possibly have any objection in reason to the following suggestions:

(1) The question of tax evasion has been rightly exercising the Finance Ministry for a number of years. Tax evasion not only corrupts our public life and civil administration by making black money available for bribes, but it also poisons the well-spring of democracy by serving as the main source of finance for political parties at election time. There should be a law making it obligatory on every political party to make a public disclosure of all donations received, particularly donations in cash. Non-disclosure should be punishable with heavy penalties, as heavy as those prescribed for tax evaders. Section 293-A of the Companies Act which prohibits donations by companies for political purposes should be repealed, since open donations which are published in the accounts are far preferable to the present practices which are a matter of common knowledge.

(2) As regards the agricultural sector, the Budget displays a strange sense of social justice. The annual national income from agriculture is about Rs. 16,000 crores, while the total income of the non-agricultural sector is roughly the same. Agricultural income-tax levied by the States totals only Rs. 13 crores, while the burden of income-tax levied by the Union on non-agricultural income will be Rs. 1,060 crores next year. Land revenue is really not to be added to agricultural income-tax in the context of this discussion. But, in any event, the land revenue collected throughout India comes to about Rs. 120 crores only. In addition to such feather-bedding of the agricultural sector, the Union proposes to give food subsidies to farmers amounting to Rs. 100 crores. The Grants-in-Aid given by the Centre under the last year's Budget to the States and the Union Territories on revenue account totalled Rs. 783 crores, and these Grants are proposed to be increased next year to Rs. 880 crores. This is a measure of the grossly unfair pressure exerted by the farm lobby within Parliament, resulting in the ever increasing burden on the urban classes who are expected to serve meekly as tax-gatherers for the Union Government.

The strident injustice to the urban population cries aloud for redress, and there are two ways of remedying it. First, the Grants-in-Aid given by the Centre to the States on revenue account must be substantially reduced, so as to compel the States to levy agricultural income-tax. To the extent of such reduction, relief from Union taxation should be given to income-tax payers. The other alternative is that since the Ruling Party has an overwhelming majority in most of the States, the State Legislatures should be made to pass resolutions under Article 252 of the Constitution enabling the Union to legislate in respect of taxation on agricultural income. After such resolutions are passed, the patently unfair distinction between agricultural and non-agricultural income can be abolished and the Union can levy reasonable rate of taxation on argricultural and non-agricultural incomes combined. That part of the income-tax collection which pertains to agricultural income could then be handed over to the States, and to this extent the burden on the Union to make Grants-in-Aid to the States on revenue account would be reduced.

(3) Our scarce financial resources should not be wasted on ideological preferences which envisage a dichotomy between the public sector and the private sector. The Government and the people should think of only one sector — the national sector. The lines of demarcation should be between efficient business and inefficient business, and between honest enterprise and dishonest enterprise. Every effort must be made to encourage and expand the first and to condemn and constrict the second, irrespective of the question whether the enterprise is in public, private or joint sector. If the same standards of economy, efficiency and managerial competence and the same criterion of dedicated public service are applied to the public

sector as well as to the private sector, we shall have achieved the greatest economic transformation of our time.

The fanatical devotion to nationalisation as an end in itself and the confluence of all controls in the hands of the Government made Galbraith observe that in the old days the principal enemy of public enterprise was those who disapproved of socialism; while now it is the socialists themselves. Contrasting India with other under-developed countries, Galbraith further remarked that there is a richness in the poverty of Indians. Unfortunately, while there is richness in our poverty, there is poverty in our socialism.

"Free Enterprise was born with man and shall survive as long as man survives."

—A. D. Shroff

(1899–1965)

Founder-President,

Forum of Free Enterprise.

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